2004-2005

Budget

Budget Plan

Québec

March 30, 2004

Finances Québec

2004-2005 Budget
Budget Plan

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2004-2005 Budget Plan

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The Québec Economy: Recent Developments and Outlook for 2004 and 2005

This section presents the economic forecasts used to prepare the 2004-2005 Budget.

Highlights

2003 was marked by a slight recovery in the global economy, more specifically in Asia and the United States. After growing 1.9% in 2002, global economic activity increased 2.5% in 2003.

Despite the favourable global climate, the economic slowdown in Québec that started in the second half of 2002 worsened in 2003. Real GDP growth was down from 4% in 2002 to 1.7% in 2003.

The slowdown is essentially due to weak U.S. demand for Québec products and strong growth in international imports, primarily as a result of the surge in the Canadian dollar. It also flows from specific factors, such as the termination of activities at the General Motors plant in Boisbriand, the closure of borders to Canadian beef due to the Alberta case of mad cow disease and the softwood lumber dispute.

Québec's weak exports were offset by continued robust domestic demand, as witnessed by the sustained growth in household consumption, residential construction and business nonresidential investment during 2003.

Québec economic activity is expected to be more vigorous in 2004 and 2005. Growth in nonresidential investment and exports to the United States will offset a more moderate household demand. Québec economic growth should reach 2.7% in 2004 and 2.9% the following year.

Global Economic and Financial Situation

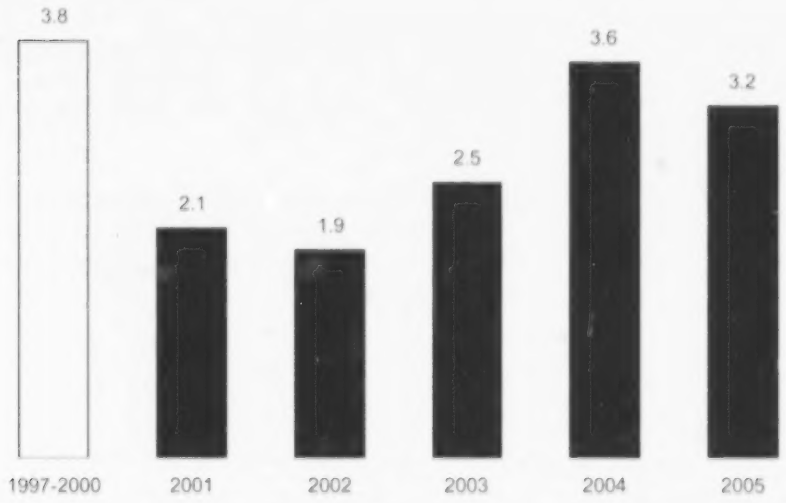
More vigorous global economic activity in 2004

After a weak 1.9% growth in real GDP in 2002, global economic activity rebounded slightly in 2003, buoyed by the positive impacts of the expansionary monetary and fiscal policies of several regions and by the particularly dynamic economic activity in Asia and the United States. However, the upswing was curtailed by the deterioration in Europe's economic climate, which was affected by the budgetary difficulties of numerous countries and Germany's economic problems. As a result, global GDP growth was 2.5% in 2003.

In 2004, the global economy will benefit from the robust U.S. and Asian economies and an improvement in Europe's economic situation. In particular, the Chinese economy, sustained by massive investment, will continue to grow at a rate of over 8% and become a key engine of global economic growth, which will reach 3.6%.

GRAPH 1.1

STRONG GLOBAL ECONOMIC GROWTH IN 2004
(real GDP, average annual percentage change)



Sources: International Monetary Fund and Consensus Economics

In 2005, a gradual hike in interest rates by several central banks and more moderate growth in the U.S. economy will slow global economic growth slightly to 3.2%.

Japan benefits from the vigorous Chinese economy

Following a slight decrease of 0.3% in real GDP in 2002, the Japanese economy improved substantially in 2003, growing 2.7%. Japan benefited from strong Chinese demand for its capital goods, stimulating Japanese firms to increase their investments. Thus, after falling 7% in 2002, investment in machinery and equipment rose 9.1% in 2003.

However, Japan's economic activity is expected to slow to 2.2% in 2004 and 1.7% in 2005 due to slightly more moderate growth in the Chinese economy and unsolved structural problems, including persistent deflation and a financial system that still needs to be restored.

TABLE 1.1

GLOBAL ECONOMIC OUTLOOK
(real GDP, percentage change)

	2002	2003	2004	2005
Japan	-0.3	2.7	2.2	1.7
China	8.0	9.1	8.3	7.7
European Union	1.1	0.8	2.0	2.2
- including Germany	0.2	-0.1	1.7	1.8
United States	2.2	3.1	4.3	3.4
Canada	3.3	1.7	3.0	3.1

Sources: Consensus Economics and ministère des Finances du Québec.

Improvement in Europe's economic situation

After reaching only 1.1% in 2002, economic growth in the European Union slowed to 0.8% in 2003. Growth was limited due to continued appreciation of the euro, which began in 2002 and contributed to a deterioration in the trade balance. As well, the *Stability and Growth Pact* made it harder for governments to introduce additional stimuli. Germany, in particular, which accounts for 23% of the European Union's economy, experienced a recession in 2003 and is still being affected by unresolved structural problems, including an ageing industrial sector.

An acceleration in economic activity elsewhere in the world is expected to offset the relatively strong euro and stimulate European exports. This foreign demand will gradually bolster domestic demand, strengthening European economic activity starting in 2004. Thus, 2% and 2.2% economic growth rates are forecast for 2004 and 2005, respectively.

Economic recovery strengthens in the United States

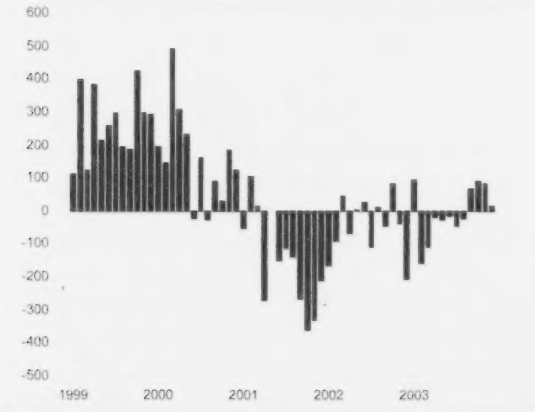
Following moderate growth of 2.2% in 2002, U.S. economic activity picked up in 2003, growing 3.1%.

A moderate upturn in investment, major fiscal stimuli that sustained household spending on durable goods, and a substantial increase in military spending all had a positive impact on the U.S. economy. Where military spending is concerned, the defence budget has swelled by US$100 billion since 2002, notably to finance the war in Iraq.

However, the dynamism of the economy has still not enabled the United States to create new jobs. In fact, more than a million jobs were lost between the end of the last recession in November 2001 and August 2003. Employment has since grown, albeit only moderately owing to the rapid rise in labour productivity, which makes it possible to produce more with fewer workers.

GRAPH 1.2

MAJOR JOB LOSSES IN THE UNITED STATES
(in thousands)



Source: Global Insight.

GRAPH 1.3

STRONG LABOUR PRODUCTIVITY GROWTH IN THE UNITED STATES
(annual percentage change)

Source: Global Insight.

Stimulated by the impact of highly expansionary monetary and fiscal policies, U.S. firms will replace the government as a driver of the economy starting in 2004, while households will benefit from gradual employment expansion.

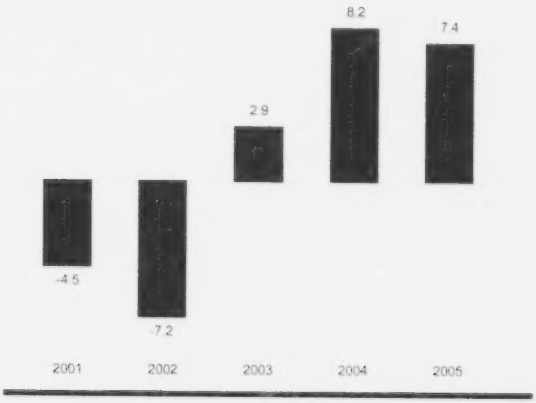
More specifically, U.S. firms will see an improvement in their financial situation and benefit from the tax incentives introduced by the Bush administration until 2005, notably the accelerated depreciation of charges associated with new investment. Business fixed investment should therefore be up 8.2% in 2004 and 7.4% in 2005.

Real U.S. GDP growth is therefore expected to be 4.3% in 2004, close to the rate observed in the late 1990s, when the U.S. economy gained from considerable investment in new technologies.

The projected increase should occur even if the federal government, grappling with a major budgetary deficit estimated at close to 4% of GDP in 2003, considerably moderates its spending growth, which is expected to be around 1.5% (in real terms) in 2005.

GRAPH 1.4

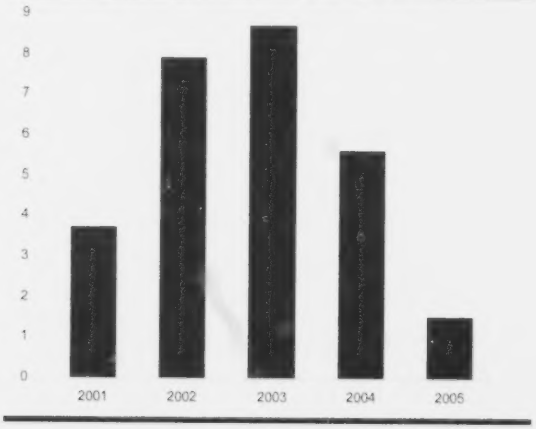
SIGNIFICANT INCREASE IN NONRESIDENTIAL INVESTMENT IN THE UNITED STATES
(constant dollars, percentage change)



Sources: Global Insight and ministère des Finances du Québec.

GRAPH 1.5

MORE MODERATE GROWTH IN SPENDING BY THE U.S. GOVERNMENT
(constant dollars, percentage change)



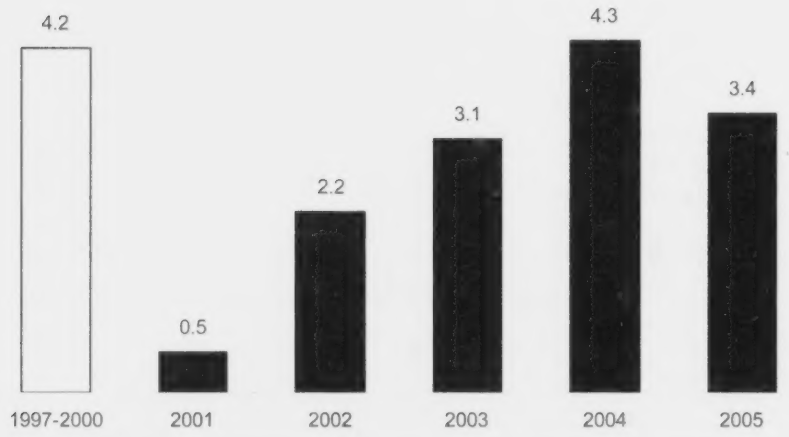
Sources: Global Insight and ministère des Finances du Québec.

However, as the benefits of the economic stimuli introduced since 2001 wear off, the impact of the structural problems in the U.S. economy will increase. In particular, the country still has to deal with high household indebtedness and major trade and federal government deficits.

Consequently, economic growth is expected to slow to 3.4% in 2005, a rate close to the potential growth in U.S. production.

GRAPH 1.6

VIGOROUS GROWTH IN THE U.S. ECONOMY IN 2004
(real GDP, average annual percentage change)



Sources: Global Insight and ministère des Finances du Québec.

Canada's economy affected by the strong dollar

Unlike its neighbour to the south, Canada experienced an economic slowdown in 2003. After reaching 3.3% in 2002, real GDP grew at a rate of only 1.7%. The slowdown is primarily attributable to the substantial appreciation of the Canadian dollar relative to the U.S. dollar, which contributed to limiting demand for Canadian products and rendered American-made products more affordable for Canadians.

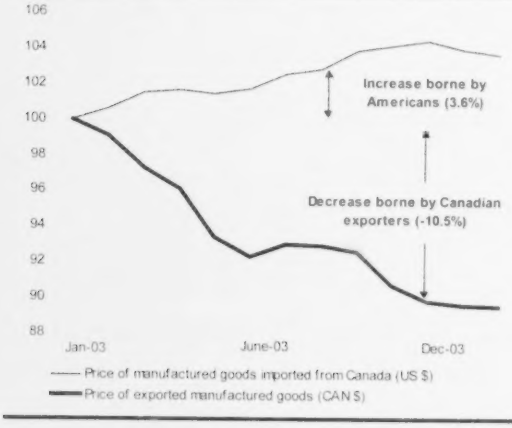
The value of the loonie rose substantially in 2003 due to favourable gaps between Canadian and U.S. interest rates, a generally weak U.S. dollar and strong global demand for Canadian raw materials. To offset the sudden rise in the dollar's value and maintain their competitive edge, Canadian manufacturers have lowered the price of their exports by 10.5% since January 2003. This adjustment made it possible to limit the increase in the price of Canadian products on U.S. markets to 3.6%.

A number of specific factors also affected demand for Canadian goods and services during the year, including the case of mad cow disease discovered in Alberta, the SARS outbreak and power failure in Ontario and the softwood lumber dispute.

The economic slowdown, which resulted in surplus productive capacity beginning in spring 2003, coupled with the higher Canadian dollar, also helped get inflation down close to the low end of the Bank of Canada's 1-3% target band.

GRAPH 1.7

EXPORTERS ABSORBED MUCH OF THE IMPACT OF THE HIGHER CANADIAN DOLLAR
(January 2003 = 100)



Sources: Statistics Canada and Bureau of Labor Statistics.

GRAPH 1.8

INFLATION ONCE AGAIN BELOW THE BANK OF CANADA TARGET BAND
(annual percentage change in consumer price index[1])

[1] *Bank of Canada reference index.*
Source: Statistics Canada.

The Bank of Canada changed the direction of its monetary policy in 2003. After twice raising the overnight interest rate by 0.25% in spring 2003 and announcing its intention to continue along this path, the Bank lowered the rate by 0.25% four times beginning in the second half of the year to 2.25% in March 2004.

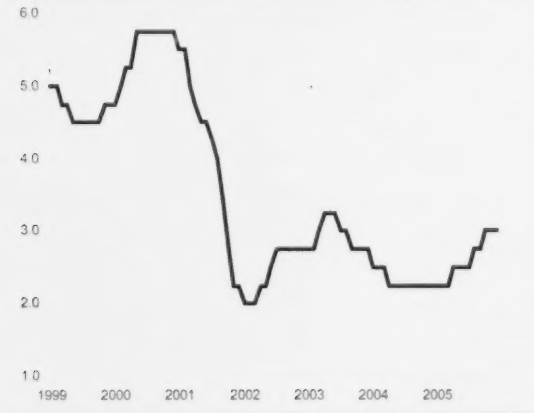
Given the still-uncertain economic recovery, surplus productive capacity and relatively strong Canadian dollar, the Bank of Canada should leave its target rate unchanged until spring 2005. After that, the Bank is expected to gradually increase interest rates as the gap between the actual and potential production levels narrows.

Thus, as interest rate gaps narrow and surplus productive capacity in the United States decreases, the Canadian dollar will gradually fall to a level that is more in line with its long-term economic determinants.

Overall, despite the high value of the loonie, Canada's economy should grow at a faster pace in 2004, reaching 3%. Dissipation of the adverse effects of the specific factors that affected the economy in 2003 and faster economic growth in the United States will spur a rebound in exports, bolstering the Canadian economy. In 2005, the lower dollar will make Canadian products more competitive on the U.S. market, thereby offsetting the slowdown in U.S. economic activity. Economic growth is expected to be 3.1%.

GRAPH 1.9

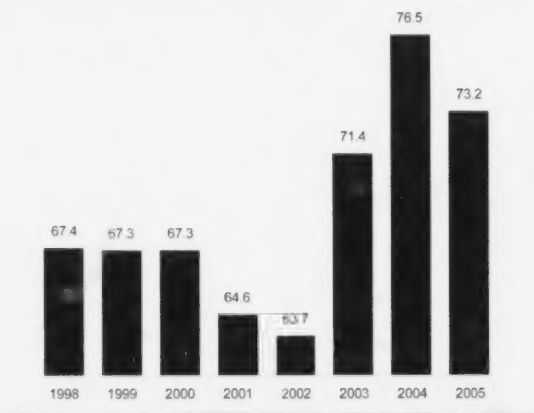
GRADUAL INCREASE IN INTEREST RATES BEGINNING IN 2005
(overnight rate, in percent)



Sources: Bank of Canada and ministère des Finances du Québec.

GRAPH 1.10

CONSIDERABLE APPRECIATION OF THE CANADIAN DOLLAR IN 2003 AND 2004
(US cents)



Sources: Bank of Canada and ministère des Finances du Québec.

Québec's Economic Record in 2003

The economy picks up

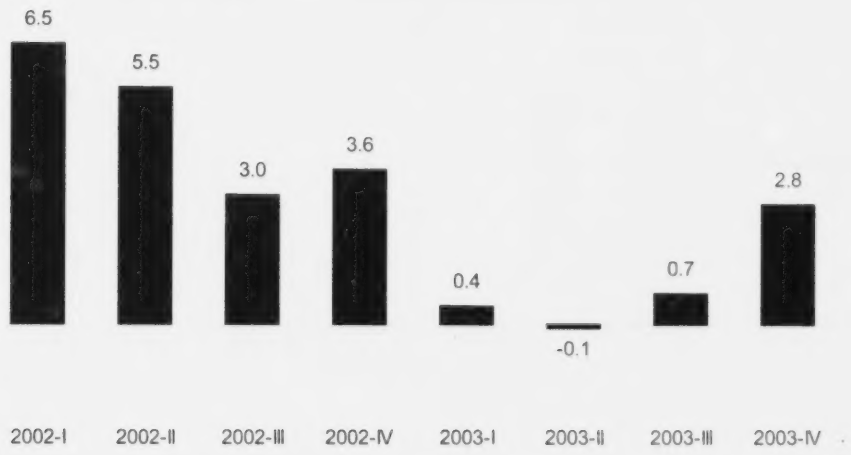
Despite dynamic domestic demand in 2003, Québec's economy was severely affected by the downturn in the external sector. The economic slowdown that started in 2002 worsened in 2003, with the economy even dipping 0.1% during the second quarter. Starting in the third quarter, however, economic activity picked up, bolstered in particular by a rebound in residential and nonresidential construction investment.

As with Canada as a whole, the considerable appreciation of the Canadian dollar relative to the U.S. dollar and the existence of specific factors hindered Québec export growth. Moreover, the high Canadian dollar made foreign products more affordable, resulting in a substantial increase in imports.

For 2003 as a whole, the Québec economy rose 1.7%, compared with 4% growth the previous year. Québec created 57 200 new jobs in 2003, a performance similar to that of the past ten years.

GRAPH 1.11

QUÉBEC ECONOMIC ACTIVITY PICKS UP
(real GDP, annualized percentage change)



Source: Institut de la statistique du Québec.

Exports decline for the third year in a row

Québec benefited little from the rebound in the U.S. economy in 2003. Already affected by weak foreign demand in major export sectors, such as industrial machinery, Québec's economy was impacted by the higher Canadian dollar. The appreciation in the dollar led, in particular, to higher U.S. prices for our products, which contributed to lower demand.

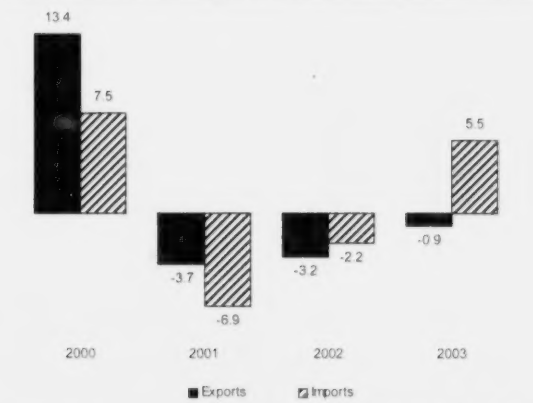
Québec export firms were forced to lower their prices and reduce their profit margins in order to maintain their sales volume. At the same time, foreign products became more affordable, thereby fostering 5.5% growth in imports to the detriment of Québec products.

Québec exports were also curtailed in 2003 by a number of specific factors, including the closing of the General Motors plant in Boisbriand in fall 2002, the case of mad cow disease discovered in Alberta, which put a stop to beef exports, the trade dispute over softwood lumber and the war in Iraq and the SARS outbreak in Ontario, which weakened the tourism industry.

Thus, in 2003, Québec exports declined 0.9%, the third year in a row that exports have fallen. The manufacturing sector was the hardest hit, suffering a decrease in shipments and jobs.

GRAPH 1.12

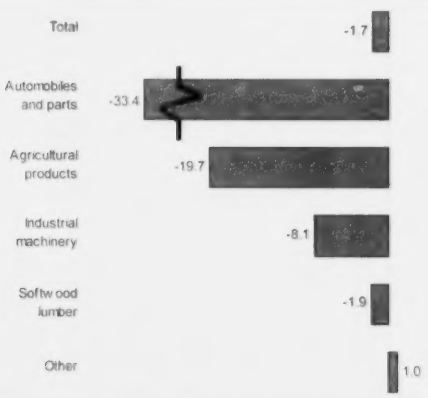
MAJOR DECLINE IN INTERNATIONAL TRADE OF QUÉBEC GOODS AND SERVICES
(constant dollars, percentage change)



Source: Institut de la statistique du Québec, based on the Québec Economic Accounts.

GRAPH 1.13

SEVERAL SECTORS AFFECTED BY SPECIFIC FACTORS IN 2003
(constant dollars, percentage change)



Source: Institut de la statistique du Québec, commodity exports on a Customs basis.

Domestic demand nevertheless remains dynamic

Domestic demand climbed 3.5% in 2003, after jumping 3.8% in 2002. High household and business confidence and low interest rates led to vigorous growth in consumer spending, housing starts and investment.

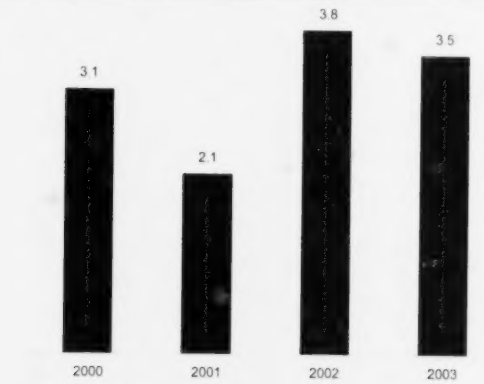
The residential construction sector, in particular, performed remarkably well in 2003, with 50 300 new housing starts: Québec's best performance in 15 years. Activity in the housing market remained very vigorous owing primarily to low mortgage rates and the low vacancy rate for rental units.

In addition, after dropping for two years, business nonresidential investment picked up again in 2003, growing 2.3%. The recovery is mainly attributable to high industrial capacity utilization, a significant increase in Hydro-Québec investments and the higher Canadian dollar, which lowered the cost of imported machinery and equipment.

GRAPH 1.14

DYNAMIC DOMESTIC DEMAND IN QUÉBEC

(constant dollars, percentage change)

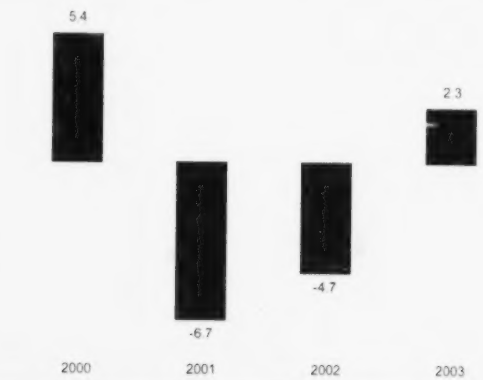


Source: Institut de la statistique du Québec.

GRAPH 1.15

REBOUND IN BUSINESS NONRESIDENTIAL INVESTMENT IN QUÉBEC IN 2003

(constant dollars, percentage change)



Source: Institut de la statistique du Québec.

Economic Outlook for Québec in 2004 and 2005

Acceleration in economic growth

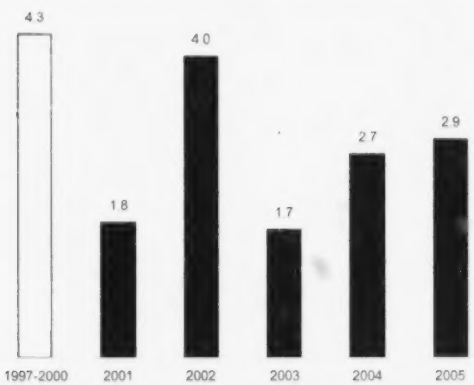
Dissipation of the specific factors that adversely affected the economy in 2003 and stronger U.S. demand for Québec products, which will gradually replace more moderate domestic demand, is expected to result in more vigorous economic activity in Québec in 2004 and 2005. Economic growth is expected to be 2.7% in 2004 and 2.9% the year after.

Gradual recovery in international exports

After sliding for the past three years, exports to the United States should start to grow as the effects of the rapid rise in the Canadian dollar during 2003 attenuate and the loonie gradually falls to its equilibrium value. Moreover, the U.S. economy will once again benefit from substantial stimuli in 2004, which will gradually spread to all economic sectors and thereby foster an upturn in Québec exports. Growth in Québec's international exports is expected to reach 3.2% in 2004 and accelerate to 5.1% in 2005.

GRAPH 1.16

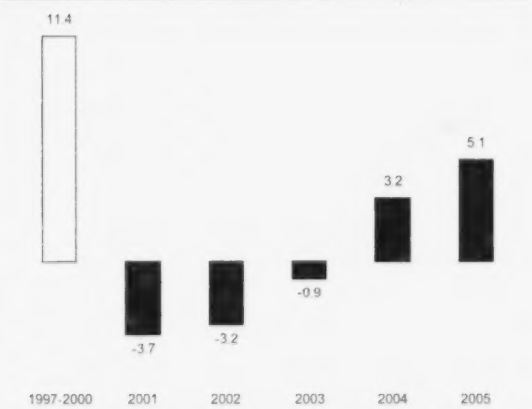
ACCELERATION OF QUÉBEC ECONOMIC GROWTH
(real GDP, average annual percentage change)



Sources: Institut de la statistique du Québec and ministère des Finances du Québec.

GRAPH 1.17

RECOVERY IN QUÉBEC'S INTERNATIONAL EXPORTS
(constant dollars, average annual percentage change)



Sources: Institut de la statistique du Québec and ministère des Finances du Québec.

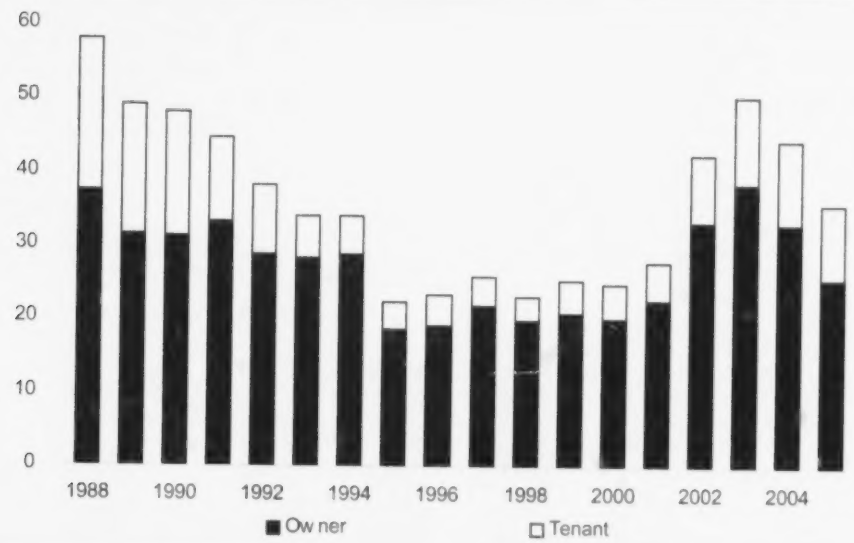
Domestic demand growth slows down

Whereas the external sector will enjoy vigorous growth, domestic demand will grow more slowly owing largely to higher interest rates and more moderate growth in job creation and government spending. However, the context will be conducive to strong growth in nonresidential investment, particularly with the continuation of major projects under way.

Despite the favourable economic conditions in the residential sector, such as the low vacancy rate, the limited housing availability on the resale market and higher prices for existing houses, housing starts will decline after two years of exceptional growth. Slower household formation and a gradual rise in interest rates will reduce the number of new housing units built. Consequently, the number of housing starts is expected to fall from 50 300 new units in 2003 to 44 400 in 2004 and 35 800 in 2005, which is still high compared with the average number of housing starts in the 1990s (around 30 000 units).

GRAPH 1.18

SLIGHT DOWNTURN IN QUÉBEC HOUSING STARTS
(in thousands of units)



Sources: Canada Mortgage and Housing Corporation and ministère des Finances du Québec.

Similarly, faced with a higher debt load and more moderate growth in their disposable income, households will consume at a slower rate. Moreover, with fewer housing units being built, household spending on durable goods will decline. After climbing 4.9% in 2003, consumer spending is expected to rise 4.1% in 2004 and 4.2% in 2005.

Furthermore, the current conditions are conducive to an upturn in investments. While several sectors have a high industrial capacity utilization rate, a higher Canadian dollar lowers the cost of machinery and equipment, over 70% of which is imported.

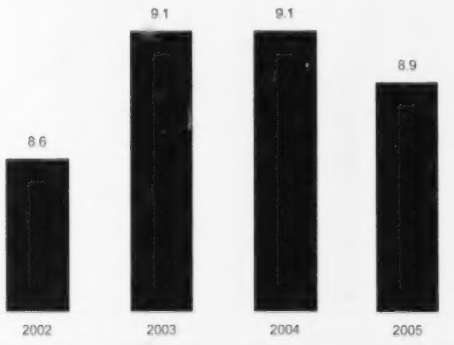
Thus, after 2.3% growth in 2003, business nonresidential investment will jump another 9% in 2004. In particular, oil refineries will be upgrading their facilities between now and 2005 in order to meet new environmental standards, whereas Hydro-Québec will accelerate its spending on construction of hydroelectric complexes to meet the increased demand.

Job creation continues

On the labour front, the predicted economic growth will enable the creation of 54 000 new jobs in 2004 and 51 000 in 2005. This will continue to foster an increase in the number of people seeking employment, which should raise the labour force participation rate to 66.4% in 2005. As a result of the higher participation rate, the unemployment rate is expected to hold steady at 9.1% on average in 2004 before falling to 8.9% the year after.

GRAPH 1.19

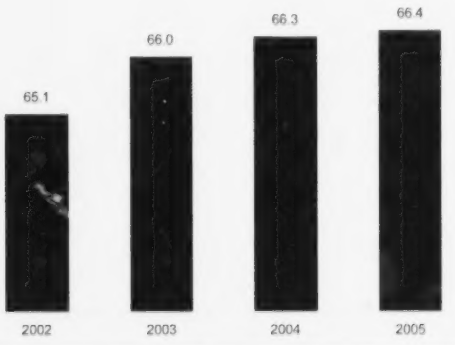
SLIGHT DECLINE IN QUÉBEC'S UNEMPLOYMENT RATE
(in percent)



Sources: Statistics Canada and ministère des Finances du Québec.

GRAPH 1.20

CHANGE IN THE LABOUR FORCE PARTICIPATION RATE IN QUÉBEC
(in percent)



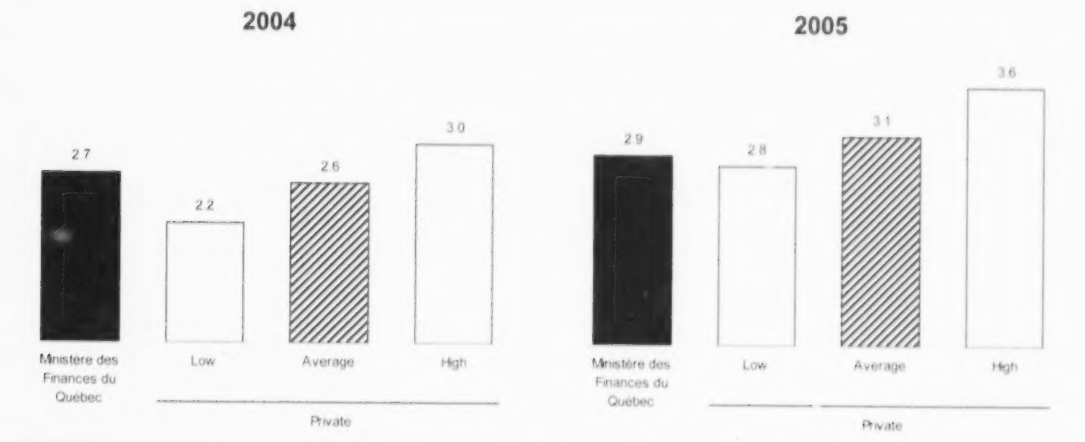
Sources: Statistics Canada and ministère des Finances du Québec.

Comparison with Private-Sector Forecasts

At 2.7%, the 2004-2005 Budget's economic growth forecast for 2004 is essentially the same as private-sector forecasts, while the 2.9% growth forecast for 2005 is slightly lower than private-sector forecasts.

GRAPH 1.21

ECONOMIC FORECAST SIMILAR TO THE PRIVATE SECTOR
(real GDP, percentage change)



Source: Ministère des Finances du Québec.

TABLE 1.2

ECONOMIC OUTLOOK FOR QUÉBEC
(percentage change)

	2003	2004	2005
OUTPUT			
— Real gross domestic product	1.7	2.7	2.9
— Gross domestic product	5.2	4.3	4.0
COMPONENTS OF EXPENDITURE			
— Consumption	4.9	4.1	4.2
— Housing starts (in thousands)	50.3	44.4	35.8
— Business nonresidential investment[1]	2.3	9.0	2.8
— International exports[1]	-0.9	3.2	5.1
COMPONENTS OF INCOME AND PRICES			
— Wages and salaries	3.9	4.0	3.9
— Personal income	3.4	4.4	3.9
— Corporate profits	8.4	3.9	3.7
— Consumer prices	2.5	1.4	1.7
LABOUR MARKET			
— Labour force	2.2	1.4	1.2
— Employment	1.6	1.5	1.4
— in thousands	57	54	51
— Unemployment rate[2]	9.1	9.1	8.9
FINANCIAL MARKETS – CANADA			
— 3-month Treasury bills[2]	2.9	2.2	2.7
— 10-year federal bonds[2]	4.8	4.8	5.2
— Exchange rate (Canadian dollar in US cents)	71.4	76.5	73.2

1 In constant 1997 dollars.
2 In percent.

Section 2

The Government's Financial Position in 2003-2004 and Public Sector Borrowings

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The government's financial transactions[1]

In accordance with the objectives of the government, a balanced budget was achieved in 2003-2004, prior to consideration of the exceptional losses of the Société générale de financement du Québec (SGF). Taking into account these additional losses, the deficit stands at $364 million.

The revenue of the Consolidated Revenue Fund for fiscal 2003-2004 is revised to $52 201 million, $317 million less than anticipated in the June 12, 2003 Budget. Own-source revenue is adjusted downward by $506 million, while federal transfers are adjusted upward by $189 million.

The expenditure of the Consolidated Revenue Fund amounts to $52 468 million in 2003-2004, a downward revision of $194 million compared with the forecast of June 12, 2003. This revision corresponds to the decline in debt service. The program spending objective of $45 800 million was met.

Consolidated net financial requirements are revised to $1 433 million, a decrease of $390 million. The net financial requirements of consolidated organizations thus amount to $1 233 million and those of the Consolidated Revenue Fund to $200 million, a downward revision of $100 million compared with the June 12, 2003 Budget. This revision can be attributed to an additional dividend of $100 million from Loto-Québec.

With respect to consolidated financing transactions, the change in direct debt is adjusted upward by $1 265 million compared with the forecast of last June.

1 **New presentation of budgetary transactions**

Sections 2 and 4 of the Budget Plan have been revised to simplify the presentation of the government's financial framework. The budgetary transactions of the Consolidated Revenue Fund, which include the profits of government enterprises, are presented separately from those of consolidated organizations. In addition, the budgetary transactions of consolidated organizations are grouped under the new heading "net results of consolidated organizations".

TABLE 2.1

GOUVERNEMENT DU QUÉBEC
SUMMARY OF CONSOLIDATED FINANCIAL TRANSACTIONS
(millions of dollars)

	2002-2003	2003-2004		
	Actual results	Budget Speech of June 12, 2003	Preliminary results	Change compared with Budget
Budgetary transactions of Consolidated Revenue Fund[1]				
Own-source revenue before exceptional losses of SGF	41 197	43 330	42 824	- 506
Federal transfers	8 932	9 188	9 377	189
Total revenue	50 129	52 518	52 201	- 317
Program spending	- 44 316	- 45 800	- 45 800	—
Debt service	- 6 536	- 6 862	- 6 668	194
Total expenditure	- 50 852	- 52 662	- 52 468	194
Net results of consolidated organizations[1]	368	144	267	123
Consolidated budget balance before exceptional losses of SGF	**- 355**	**0**	**0**	**0**
Exceptional losses of SGF	- 339	—	- 364	- 364
Consolidated budget balance	**- 694**	**0**	**- 364**	**- 364**
Consolidated non-budgetary transactions				
Investments, loans and advances	- 1 649	- 1 814	- 1 077	737
Capital expenditures	- 1 482	- 1 334	- 978	356
Retirement plans	2 007	2 041	2 221	180
Other accounts	240	- 716	- 1 235	- 519
Consolidated non-budgetary requirements	**- 884**	**- 1 823**	**- 1 069**	**754**
Consolidated net financial requirements	**- 1 578**	**- 1 823**	**- 1 433**	**390**
Consolidated financing transactions				
Change in cash position[2]	- 3 090	4 110	2 466	- 1 644
Change in direct debt[2]	6 309	66	1 331	1 265
Retirement plans sinking fund[3]	- 1 641	- 2 353	- 2 364	- 11
Total financing of consolidated transactions	**1 578**	**1 823**	**1 433**	**- 390**

Note: A negative entry indicates a financial requirement and a positive entry, a source of financing. For the change in cash position, a negative entry indicates an increase and a positive entry, a decrease. For purposes of comparison, the data are presented on the basis of the 2004-2005 budgetary structure. Because of the changes that will be made in the family policy as of January 1, 2005, amounts previously included in program spending will be applied against revenue. The data presented in this section incorporate a restatement that covers a three-month period and that reduces own-source revenue and program spending by $132 million. Therefore, the restatement does not change the budget balance for the years concerned.

1 The budgetary transactions of the Consolidated Revenue Fund, which include the profits of government enterprises, are presented separately from those of consolidated organizations. In addition, the budgetary transactions of consolidated organizations are grouped under the new heading "net results of consolidated organizations".

2 The change in direct debt includes new long-term borrowings less repayment of long-term borrowings and the change in temporary borrowings outstanding. Previously, the change in temporary borrowings outstanding was included in the change in cash position. See the explanation of consolidated financing transactions given later in this section.

3 This sinking fund receives amounts to be used to cover retirement benefits payable by the government under the public and parapublic sector retirement plans. The investment income of this fund is reinvested in it.

Revenue of the Consolidated Revenue Fund

In regard to revenue, the 2003-2004 Budget anticipated own-source revenue of $43 330 million and federal transfers of $9 188 million. The forecast for own-source revenue before the exceptional losses of the SGF is adjusted downward by $506 million compared with the figure anticipated in the Budget, while the forecast for federal transfers is raised by $189 million.

Own-source revenue

Excluding government enterprises, the downward adjustment of own-source revenue amounts to $537 million. This adjustment reflects mainly the lower-than-expected revenue from personal income tax and corporate taxes.

TABLE 2.2

GOUVERNEMENT DU QUÉBEC – CONSOLIDATED REVENUE FUND
SUMMARY OF THE CHANGE IN OWN-SOURCE REVENUE
(millions of dollars)

	2002-2003				2003-2004
	Actual results	Budget Speech of June 12, 2003	Preliminary results	Change compared with Budget	Change compared with 2002-2003
					%
Personal income tax	16 048	16 891	16 454	– 437	2.5
Health Services Fund	4 068	4 640	4 658	18	14.5
Corporate taxes	3 735	3 926	3 837	– 89	2.7
Consumption taxes	10 843	11 567	11 596	29	6.9
Other sources	2 402	2 364	2 306	– 58	– 4.0
Sub-total before government enterprises	**37 096**	**39 388**	**38 851**	**– 537**	**4.7**
Government enterprises before exceptional losses of SGF	4 101	3 942	3 973	31	– 3.1
Total own-source revenue before exceptional losses of SGF	**41 197**	**43 330**	**42 824**	**– 506**	**3.9**

Note: Data restated according to the information provided at the bottom of Table 2.1.

The preliminary results for personal income tax indicate a decline of $437 million compared with the 2003-2004 Budget. Continued processing of 2002 income tax returns in 2003-2004 resulted in a lower-than-anticipated level of tax payable, particularly in the case of self-employed workers. It also led to a decline in tax instalments for 2003, since the latter are calculated on the basis of information for the 2002 taxation year.

Corporate tax revenue is revised downward by $89 million on account of lower-than-expected growth in the profits of corporations.

Consumption tax revenue is adjusted upward by $29 million. This rise is due primarily to higher revenue from the fuel tax because of an increase in the amount of fuel consumed. The increase in the tax on tobacco products announced last December also contributed to this adjustment.

However, revenue from other sources is revised downward by $58 million, owing in particular to lower-than-anticipated revenue from sales of goods and services, duties and permits and interest income.

Lastly, the profits of government enterprises, before the exceptional losses of the SGF, are revised to $3 973 million, an increase of $31 million compared with the forecast in the June 2003 Budget.

Exceptional losses of the Société générale de financement du Québec (SGF)

The SGF has registered losses over the past three years, and these results have a major impact on government revenue.

In 2001, the losses totalled $84 million and in 2002, $172 million. Recently, the SGF announced a loss of $511 million for 2003, stemming mainly from the complete reevaluation of its investment portfolio under the supervision of a specialized firm.

The SGF also anticipates a loss of $30 million for the first quarter of 2004.

On the basis of the government's fiscal years, these losses as a whole affected the government's results by $91 million in 2001-2002, $339 million in 2002-2003 and $364 million in 2003-2004.

TABLE 2.3

SOCIÉTÉ GÉNÉRALE DE FINANCEMENT DU QUÉBEC
IMPACT OF LOSSES ON GOVERNMENT REVENUE
(millions of dollars)

	2001-2002	2002-2003	2003-2004	Total
Losses of the SGF[1]				
2001	– 81			– 84[2]
2002	– 10	– 162		– 172
2003		– 177	– 334	– 511
2004[3]			– 30	– 30
Total	– 91	**– 339**	**– 364**	**– 797**

1 The SGF's fiscal year corresponds to the calendar year.
2 Including a loss of $3 million charged to the government's 2000-2001 fiscal year.
3 Anticipated losses from January to March 2004.

Federal transfers

Federal transfers should reach $9 377 million for fiscal 2003-2004, an increase of $189 million compared with the forecast in the 2003-2004 Budget. However, without the deferral and spreading mechanism introduced by the federal government, revenue from federal transfers would have been revised downward by $972 million in 2003-2004.

TABLE 2.4

GOUVERNEMENT DU QUÉBEC – CONSOLIDATED REVENUE FUND
SUMMARY OF THE CHANGE IN FEDERAL TRANSFERS
(millions of dollars)

	2002-2003				2003-2004
	Actual results	Budget Speech of June 12, 2003	Preliminary results	Change compared with Budget	Change compared with 2002-2003
					%
Equalization	5 315	4 145	4 065	– 80	– 23.5
Canada Health and Social Transfer (CHST)	2 648	4 133	4 266	133	61.1
Other transfers related to fiscal arrangements	34	15	64	49	88.2
Other programs	935	895	982	87	5.0
Total federal transfers	**8 932**	**9 188**	**9 377**	**189**	**5.0**
Less:					
Impact of the deferral mechanism introduced by the federal government	—	—	1 161	1 161	—
Total federal transfers before deferral	**8 932**	**9 188**	**8 216**	**– 972**	**– 8.0**

Equalization revenue is revised downward by $80 million compared with the forecast in the 2003-2004 Budget. The final data compiled by Canada Revenue Agency (CRA) in regard to personal income tax and corporate taxable income lead to a major upward adjustment of Québec's fiscal capacity in relation to that of the provinces that make up the equalization program's standard. These new data thus entailed to a downward adjustment of over $1 billion in equalization revenue, including $771 million solely in respect of tax on corporate profits. However, on account of the scope of these adjustments, the federal government has allowed repayment of the major portion, i.e. $1 074 million, to be deferred and spread over a five-year period starting in 2005-2006.

Revenue from the Canada Health and Social Transfer (CHST) is adjusted upward by $133 million. A review of the value of the tax points used to calculate the CHST resulted in an increase in cash transfers. In addition, the deferral mechanism introduced by the federal government raised CHST revenue by $87 million.

The $49-million rise in other transfers related to fiscal arrangements reflects the outstanding growth of revenue from tax on preferred shares in 2002.

The $87-million revision in regard to other programs stems mainly from a reevaluation of the increase in revenue respecting immigrant integration agreements, the federal student loan program and services for people with hepatitis C.

Measure aimed at deferring repayment of part of the decrease in federal transfers in 2003-2004

Federal transfers were to have fallen by 8.0% in 2003-2004. Indeed, a 43.7% decline in equalization revenue would have more than offset the climb in CHST revenue stemming from the federal government's February 2003 announcement on health care.

However, the federal government has allowed Québec and the other provinces to defer repayment of the downward adjustments to equalization and the CHST resulting from the updating of population data and personal income tax and corporate income tax data between the federal estimates of October 2003 and February 2004. These adjustments total $1 161 million in 2003-2004. Repayments will be made over a five-year period starting in 2005-2006, at a rate of $244 million per year.

TABLE 2.5

GOUVERNEMENT DU QUÉBEC – CONSOLIDATED REVENUE FUND IMPACT OF THE DEFERRAL OF PART OF THE ADJUSTMENTS TO FEDERAL TRANSFERS IN 2003-2004
(millions of dollars)

	2002-2003	2003-2004		
		Before deferral	Deferral	After deferral
Equalization	5 315	2 991	1 074	4 065
% change		– 43.7	—	– 23.5
CHST	2 648	4 179	87	4 266
% change		57.8	—	61.1
Other	969	1 046	—	1 046
% change		7.9	—	7.9
Total	**8 932**	**8 216**	**1 161**	**9 377**
% change		**– 8.0**	**—**	**5.0**

Expenditure of the Consolidated Revenue Fund

Expenditure for fiscal 2003-2004 was revised downward by $194 million to $52 468 million. This decrease corresponds to the decline in debt service.

In all, program spending rose 3.3% compared with 2002-2003, while debt service climbed 2%.

TABLE 2.6

GOUVERNEMENT DU QUÉBEC – CONSOLIDATED REVENUE FUND
SUMMARY OF THE CHANGE IN EXPENDITURE
(millions of dollars)

	2002-2003				2003-2004
	Actual results	Budget Speech of June 12, 2003	Preliminary results	Change compared with Budget	Change compared with 2002-2003
					%
Program spending	44 316	45 800	45 800	—	3.3
Debt service					
Direct debt service	3 888	4 177	3 926	– 251	1.0
Interest ascribed to retirement plans[1]	2 648	2 685	2 742	57	3.5
Total debt service	6 536	6 862	6 668	– 194	2.0
Total expenditure	**50 852**	**52 662**	**52 468**	**– 194**	**3.2**

Note: Data restated according to the information provided at the bottom of Table 2.1.

1 Interest ascribed to the retirement plans is equal to interest on the actuarial obligation less the investment income of the retirement plans sinking fund.

The $45 800-million forecast for program spending includes spending adjustments made during fiscal 2003-2004. Additional spending was incurred mainly at the ministère de l'Emploi, de la Solidarité sociale et de la Famille, because of the lower-than-anticipated decrease in the number of households receiving employment assistance, and at the ministère de la Sécurité publique. However, equivalent savings were realized in other departments.

Debt service currently amounts to $6 668 million, of which $3 926 million is for direct debt service and $2 742 million for interest ascribed to the retirement plans. The $194-million downward revision of debt service essentially reflects lower-than-expected interest rates.

Budgetary transactions of consolidated organizations

The net results of consolidated organizations amount to $267 million, $123 million more than forecast in the June 2003 Budget. This increase in net results is due to the allocation of adjustments among a large number of organizations.

TABLE 2.7

GOUVERNEMENT DU QUÉBEC – CONSOLIDATED ORGANIZATIONS
SUMMARY OF BUDGETARY TRANSACTIONS
(millions of dollars)

	2002-2003				2003-2004
	Actual results	Budget Speech of June 12, 2003	Preliminary results	Change compared with Budget	Change compared with 2002-2003
					%
Own-source revenue	2 160	2 035	2 194	159	1.6
Federal transfers	375	396	498	102	32.8
Total revenue	2 535	2 431	2 692	261	6.2
Expenditure excluding debt service	– 1 618	– 1 637	– 1 829	– 192	13.0
Debt service	– 549	– 650	– 596	54	8.6
Total expenditure	– 2 167	– 2 287	– 2 425	– 138	11.9
Net results	**368**	**144**	**267**	**123**	**– 27.4**

Consolidated non-budgetary transactions

Financial requirements stemming from consolidated non-budgetary transactions amount to $1 069 million, $754 million less than forecast in the Budget Speech of June 12, 2003.

TABLE 2.8

GOUVERNEMENT DU QUÉBEC
SUMMARY OF CONSOLIDATED NON-BUDGETARY TRANSACTIONS
(millions of dollars)

			2003-2004
	Budget Speech of June 12, 2003	Preliminary results	Change
Consolidated Revenue Fund			
Investments, loans and advances			
Government enterprises	– 1 305	– 604	701
Municipalities, municipal bodies, individuals, corporations and others	– 208	– 209	– 1
	– 1 513	– 813	700
Capital expenditures	– 122	– 122	—
Retirement plans	2 041	2 221	180
Other accounts	– 562	– 855	– 293
Total Consolidated Revenue Fund	**– 156**	**431**	**587**
Consolidated organizations			
Capital expenditures	– 1 212	– 856	356
Other	– 455	– 644	– 189
Total consolidated organizations	**– 1 667**	**– 1 500**	**167**
Consolidated non-budgetary requirements	**– 1 823**	**– 1 069**	**754**

Note: A negative entry indicates a financial requirement and a positive entry, a source of financing.

The preliminary results of the Consolidated Revenue Fund for investments, loans and advances show a $700-million decline in funding requirements compared with the June 2003 forecast. This difference can be attributed essentially to a $288-million reduction in investments and a decline in revenue from government enterprises.

Financial requirements for the retirement plans were $180 million less than forecast in June 2003. This improvement can be attributed mainly to the recording of expenditures not disbursed during the fiscal year, i.e. interest ascribed to the retirement plans.

Transactions related to other non-budgetary accounts represent year-to-year changes in these financial items. These accounts, which include, in particular, cash and bills on hand, outstanding cheques, accounts receivable and accounts payable, can fluctuate a great deal because of the variability of government cash inflow and disbursements. For 2003-2004, the balance of the other accounts of the Consolidated Revenue Fund entails a $293-million increase in financial requirements.

The $167-million decrease in the financial requirements of consolidated organizations can be explained by, among other things, a reduction in the level of capital investments.

Consolidated financing transactions

New presentation of short-term borrowings

The government uses long-term and short-term borrowings to meet its financial requirements. Short-term borrowings include Treasury bills and temporary borrowings. At present, Treasury bills outstanding are recorded under direct debt since Treasury bills are always renewed when they mature and are used to meet long-term financial requirements. To date, however, temporary borrowings have been presented under the cash position.

For consistency, the government's total debt should be adjusted to take into account all short-term borrowings that are used to finance long-term financial requirements. The presentation of temporary borrowings will thus be identical to that of Treasury bills. It should be noted that, at the end of the fiscal year, the Consolidated Revenue Fund does not usually have short-term borrowings other than Treasury bills.

TABLE 2.9

INCLUSION OF SHORT-TERM BORROWINGS IN TOTAL DEBT
(millions of dollars)

	1998	1999	2000	2001	2002	2003	2004[1]
Total debt as at March 31	97 732	99 572	100 546	102 741	105 172	108 526	112 019
Short-term borrowings outstanding other than Treasury bills	653	1 541	1 574	2 107	2 003	2 861	2 779
Total debt as at March 31 including short-term borrowings	**98 385**	**101 113**	**102 120**	**104 848**	**107 175**	**111 387**	**114 798**

1 Preliminary results

For purposes of comparison, the financing transactions forecast in the Budget Speech of June 12, 2003 must be revised to take the new treatment of temporary borrowings into account.

In the case of the Consolidated Revenue Fund, the $3 945-million change in cash position anticipated in the June 12, 2003 Budget Speech included a $165-million decrease in temporary borrowings outstanding. This decrease is now included as a repayment of borrowings in the change in direct debt. In the case of consolidated organizations, a $509-million increase in temporary borrowings was included in the change in cash position in the last Budget. This increase in the level of temporary borrowings is now considered new borrowings in the change in direct debt.

Financing

Preliminary results for 2003-2004 show that the change in direct debt amounts to $1 331 million, i.e. $98 million for the Consolidated Revenue Fund and $1 233 million for consolidated organizations. Borrowings in fiscal 2003-2004 amount to $7 355 million ($4 940 million for the Consolidated Revenue Fund and $2 415 million for consolidated organizations). It should be noted that the Consolidated Revenue Fund obtained pre-financing of $1 644 million that will be used to cover part of the borrowing program in 2004-2005.

TABLE 2.10

GOUVERNEMENT DU QUÉBEC
SUMMARY OF CONSOLIDATED FINANCING TRANSACTIONS
(millions of dollars)

					2003-2004
	Budget Speech of June 12, 2003	Change in temporary borrowings	Budget Speech of June 12, 2003 revised	Preliminary results	Change
Change in cash position					
Consolidated Revenue Fund	3 945	165	4 110	2 466	–1 644
Consolidated organizations	509	– 509	—	—	—
Total change in cash position	**4 454**	**– 344**	**4 110**	**2 466**	**– 1 644**
Change in direct debt					
Consolidated Revenue Fund					
New borrowings	2 608	—	2 608	4 940	2 332
Repayment of borrowings	– 3 900	– 165	– 4 065	– 4 842	– 777
	– 1 292	– 165	– 1 457	98	1 555
Consolidated organizations					
New borrowings	2 310	509	2 819	2 415 [1]	– 404
Repayment of borrowings	– 1 296	—	– 1 296	– 1 182	114
	1 014	509	1 523	1 233	– 290
Total change in direct debt	**– 278**	**344**	**66**	**1 331**	**1 265**
Retirement plans sinking fund	**– 2 353**	**—**	**– 2 353**	**– 2 364**	**– 11**
Total financing of consolidated transactions	**1 823**	**—**	**1 823**	**1 433**	**– 390**

Note: A negative entry indicates a financial requirement and a positive entry, a source of financing. For the change in cash position, a negative entry indicates an increase and a positive entry, a decrease.

1 Including an $83-million increase in temporary borrowings.

Financing of the Consolidated Revenue Fund

Preliminary results show that the change in the direct debt of the Consolidated Revenue Fund is $98 million, an increase of $1 555 million compared with the figure announced in the 2003-2004 Budget Speech. Borrowings in 2003-2004 stand at $4 940 million, $2 332 million more than expected in the last Budget, mainly on account of pre-financing of $1 644 million and the $777-million increase in the repayment of borrowings.

Owing to pre-financing, the cash level will fall by only $2 466 million, even though a $4 110-million decrease was forecast in the last Budget.

Financing of consolidated organizations

The change in the direct debt of consolidated organizations should amount to $1 233 million, $290 million less than anticipated in the last Budget.

This adjustment is due to the fact that the net financial requirements of consolidated organizations are lower than forecast.

Borrowings

In all, the government contracted long-term borrowings of $7 440 million in 2003-2004, of which $4 940 million was for Consolidated Revenue Fund needs and $2 500 million for the Financing Fund. The borrowings of the Financing Fund are used to meet the financing needs of consolidated organizations ($2 332 million) and certain government enterprises ($168 million).

In all, 97% of the financing program, or $7 231 million, was conducted in Canadian dollars. In regard to the main financial instruments used, the government carried out six public bond issues on the Canadian market for a total of $3 041 million, and real return issues for a total of $656 million. In addition, medium-term notes were issued on the Canadian market for $1 585 million, and on the European market for $498 million. In addition, private-contract financing worth $436 million was carried out with the Caisse de dépôt et placement du Québec. Lastly, savings products sold by Épargne Placements Québec should provide the government with $793 million in financing.

Only 3% of the financing program was conducted in foreign currency. A public bond issue was carried out on the Australian market for AUS$200 million (CAN$209 million) in February 2004.

TABLE 2.11

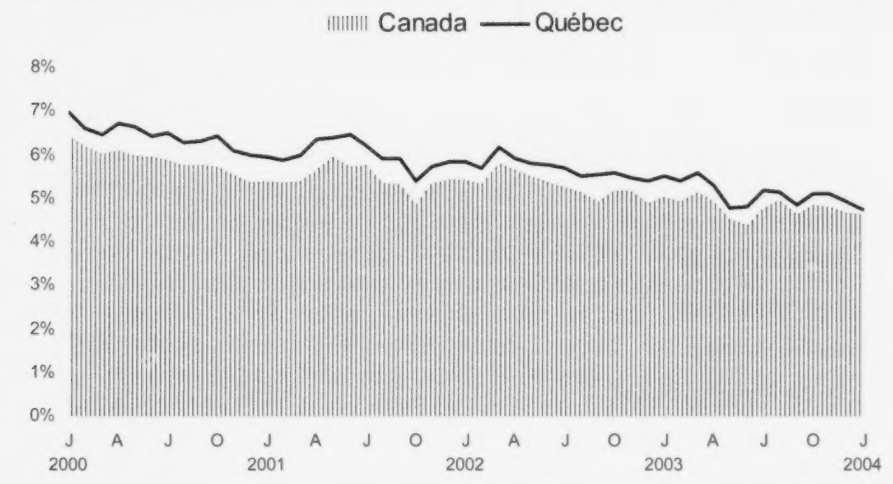
GOUVERNEMENT DU QUÉBEC
SUMMARY OF LONG-TERM BORROWINGS IN 2003-2004
(millions of dollars)

Currency	Consolidated Revenue Fund	Consolidated organizations[1]	Government enterprises	Total	
					%
Canadian dollar					
Public issues					
Negotiable bonds	1 475	1 566	—	3 041	42.1
Real return bonds	656	—	—	656	9.1
Medium-term notes					
On the Canadian market	1 585	—	—	1 585	21.9
On the European market	—	498	—	498	6.9
Private issues					
Caisse de dépôt et placement du Québec	—	268	168	436	6.0
Canada Pension Plan Investment Fund	5	—	—	5	0.1
Savings products	793	—	—	793	10.9
Immigrant Investor Program	450	—	—	450	6.2
Change in debt resulting from currency swaps	– 233	—	—	– 233	– 3.2
Sub-total	**4 731**	**2 332**	**168**	**7 231**	**97.2**
Australian dollar					
Public issue	209	—	—	209	100.0
Sub-total	**209**	—	—	**209**	**2.8**
Total	**4 940**	**2 332**	**168**	**7 440**	**100.0**

1 Excluding the $83-million increase in temporary borrowings.

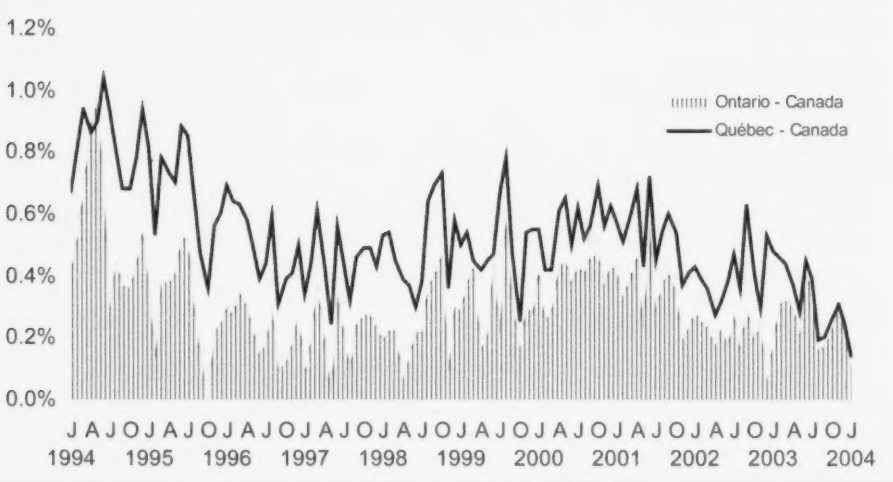
GRAPH 2.1

YIELD ON LONG-TERM (10-YEAR) SECURITIES



GRAPH 2.2

YIELD SPREAD ON LONG-TERM (10-YEAR) SECURITIES


1.2%
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0.8%
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Ontario - Canada
Québec - Canada
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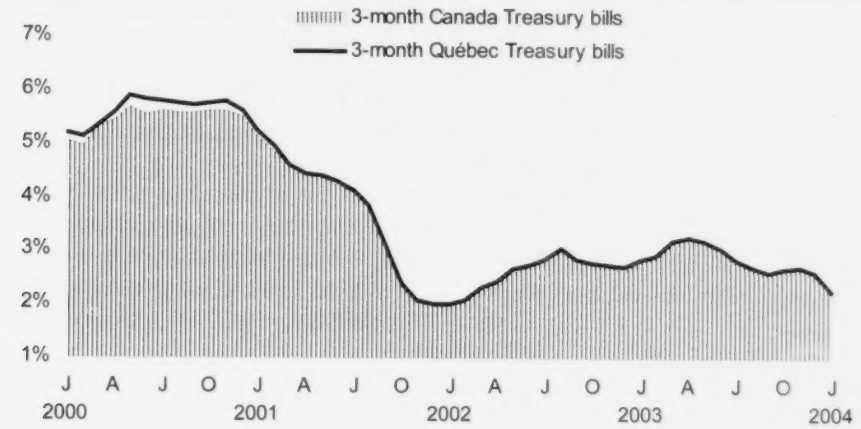
1994 1995 1996 1997 1998 1999 2000 2001 2002 2003 2004

GRAPH 2.3

YIELD ON SHORT-TERM SECURITIES



Repayment of borrowings

Preliminary results show that the repayment of borrowings of the Consolidated Revenue Fund and consolidated organizations for fiscal 2003-2004 amounts to $6 024 million, $663 million more than forecast in the June 12, 2003 Budget Speech.

Repayment of borrowings of the Consolidated Revenue Fund

Preliminary results show that the repayment of borrowings of the Consolidated Revenue Fund amounts to $4 842 million, $777 million more than forecast in the Budget Speech of last June. This increase is due in particular to higher-than-anticipated repayments of savings products and higher-than-expected revenue of the sinking fund for government borrowings.

Repayment of borrowings of consolidated organizations

Preliminary results show that the repayment of borrowings of consolidated organizations for fiscal 2003-2004 stands at $1 182 million, $114 million less than forecast in the last Budget.

Total government debt

The government's total debt consists of the consolidated direct debt and the net retirement plans liability. The consolidated direct debt is the sum of the direct debt of the Consolidated Revenue Fund and the debt of consolidated organizations. The net retirement plans liability consists of the retirement plans liability minus the balance of the retirement plans sinking fund (RPSF), an asset that will eventually be used to pay the retirement benefits of public and parapublic sector employees.

Preliminary results show that the government's consolidated direct debt amounts to $78 159 million as at March 31, 2004, or $68 692 million as direct debt of the Consolidated Revenue Fund and $9 467 million as debt of the consolidated organizations.

It should be noted that an amount of $1 644 million included in the consolidated direct debt represents pre-financing in 2003-2004 that will be used to cover part of the borrowing program in 2004-2005.

As at March 31, 2004, the net retirement plans liability stands at $38 283 million.

Excluding pre-financing, the government's total debt is $114 798 million as at March 31, 2004.

TABLE 2.12

TOTAL GOVERNMENT DEBT AS AT MARCH 31, 2004[1]
(millions of dollars)

	Consolidated direct debt				
	Consolidated Revenue Fund	Consolidated organizations	Total	Net retirement plans liability	Total debt
Debt as at March 31, 2004	68 692	9 467	78 159	52 487	130 646
Retirement plans sinking fund	—	—	—	– 14 204	– 14 204
Sub-total	**68 692**	**9 467**	**78 159**	**38 283**	**116 442**
Pre-financing	– 1 644	—	– 1 644	—	– 1 644
Total	**67 048**	**9 467**	**76 515**	**38 283**	**114 798**

1 Preliminary results.

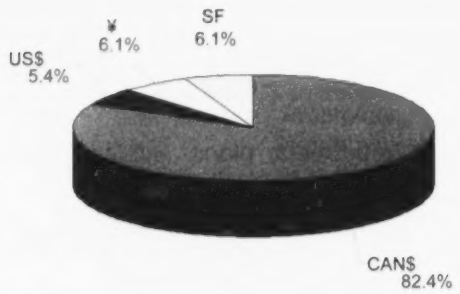
Structure of debt

As at March 31, 2004, the proportion of the direct debt of the Consolidated Revenue Fund in Canadian dollars should amount to 82.4% and the proportion in foreign currency, 17.6%. In addition, as at March 31, 2004, the share at fixed interest rates and the share at variable interest rates should be 58.4% and 41.6% respectively.

GRAPH 2.4

STRUCTURE OF THE DIRECT DEBT OF THE CONSOLIDATED REVENUE FUND AS AT MARCH 31, 2004[1]

BY CURRENCY



BY INTEREST RATE

1 Preliminary results.

Including the debt of consolidated organizations and the net retirement plans liability, the proportion of the total debt in Canadian dollars should amount to 89.6% and that in foreign currency, 10.4% as at March 31, 2004.

TABLE 2.13

STRUCTURE OF THE TOTAL DEBT AS AT MARCH 31, 2004[1]
(millions of dollars)

	Consolidated direct debt							
Currency	**Consolidated Revenue Fund**	**%**	**Consolidated organizations**	**Total**	**%**	**Net retirement plans liability**	**Total debt**	**%**
Canadian dollar	56 583	82.4	9 467	66 050	84.5	38 283	104 333	89.6
US dollar	3 689	5.4	—	3 689	4.7	—	3 689	3.2
Yen	4 210	6.1	—	4 210	5.4	—	4 210	3.6
Swiss franc	4 210	6.1	—	4 210	5.4	—	4 210	3.6
Sub-total	**68 692**	**100.0**	**9 467**	**78 159**	**100.0**	**38 283**	**116 442**	**100.0**
Pre-financing	– 1 644		—	– 1 644		—	– 1 644	
Total	**67 048**		**9 467**	**76 515**		**38 283**	**114 798**	

Note: The debt in foreign currency is expressed in the Canadian equivalent based on the exchange rates in effect on March 24, 2004.

1 Preliminary results.

Public sector borrowings, investments and debt

Public sector borrowings and investments

Preliminary results for 2003-2004 show that gross long-term public sector borrowings amount to $15 917 million.

Gross borrowings in Canadian dollars total $15 658 million, or 98.4% of total borrowings by the public sector. Gross borrowings in foreign currency total $259 million, or 1.6% of public sector borrowings as a whole.

TABLE 2.14

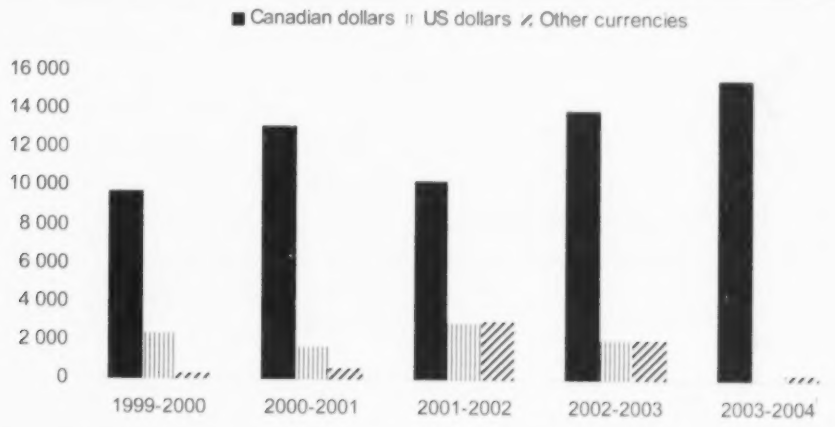
NET LONG-TERM PUBLIC SECTOR BORROWINGS
(millions of dollars)

	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004[1]
Gross borrowings					
Government[2, 3]	5 677	8 757	8 438	10 079	7 050
Educational institutions	1 366	1 540	1 179	2 012	1 213
Health and social services institutions	66	528	429	1 127	668
Hydro-Québec[4]	2 212	2 124	3 388	1 923	2 249
Other government enterprises	488	16	274	192	194
Municipalities and municipal bodies	2 594	2 488	2 595	2 880	4 543
Total gross borrowings	**12 403**	**15 453**	**16 303**	**18 213**	**15 917**
Repayment of borrowings	**12 473**	**13 103**	**13 060**	**11 275**	**13 412**
Sub-total	**– 70**	**2 350**	**3 243**	**6 938**	**2 505**
Pre-financing					
for the current year	– 506	– 1 475	– 1 154	– 3 967	– 1 644
for the previous year	2 831	506	1 475	1 154	3 967
Net long-term borrowings	**2 255**	**1 381**	**3 564**	**4 125**	**4 828**

1 Preliminary results.
2 Amounts borrowed to cover the requirements of the Consolidated Revenue Fund and consolidated organizations, excluding net amounts received under interest rate and currency swap agreements, which explains the difference between this list and the list of borrowings given later in this text. These amounts also exclude borrowings made to cover the requirements of certain government enterprises and Financement-Québec, which are distributed among the organizations and networks for which they are intended.
3 The government's gross borrowings include short-term borrowings used to finance long-term financial requirements.
4 Amounts borrowed as at December 31 of each year.

GRAPH 2.5

GROSS PUBLIC SECTOR BORROWINGS BY CURRENCY
(millions of dollars)

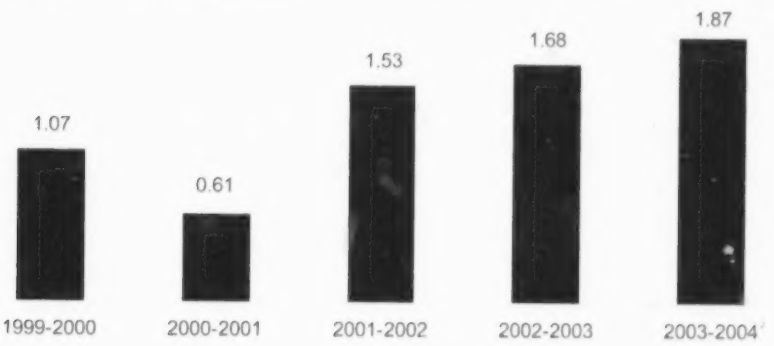


1 Preliminary results.

To ensure that borrowings in a given fiscal year are on a basis comparable with investments and gross domestic product, pre-financing must be allocated to the years to which it applies. Net long-term public sector borrowings for 2003-2004 amount to $4 828 million, an increase of $703 million compared with the previous year. Consequently, the ratio of net long-term borrowings to gross domestic product rose from 1.68% of GDP in 2002-2003 to 1.87% in 2003-2004.

GRAPH 2.6

NET LONG-TERM PUBLIC SECTOR BORROWINGS[1]
(as a percentage of GDP)



1 Adjusted by pre-financing.
2 Preliminary results.

Preliminary results show that public sector investments total $9 704 million in 2003-2004, $885 million more than the previous year. This increase can be attributed mainly to the growth in investments by Hydro-Québec. Compared with the previous year, Hydro-Québec invested $400 million more for developing its production capacity (Toulnustouc, Eastmain-1) and $200 million in its power transmission grid, particularly to reinforce the Montérégie loop.

TABLE 2.15

PUBLIC SECTOR INVESTMENTS
(millions of dollars)

	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004[1]
Government[2]	1 085	1 448	1 614	2 031	1 624
Educational institutions[3]	702	691	703	1 070	1 216
Health and social services institutions[3]	615	699	706	785	860
Hydro-Québec[4]	1 457	1 632	1 686	2 208	2 895
Other government enterprises[5]	376	666	934	960	932
Municipalities and municipal bodies[6]	1 703	1 601	1 855	1 765	2 177
	5 938	**6 737**	**7 498**	**8 819**	**9 704**

1 Preliminary results.

2 Government investments include its capital expenditures as well as grants and loans for investments made available to economic agents outside the public sector. Financial investments for other components of the public sector are therefore excluded. Government investments also include investments by consolidated organizations.
Sources: Public accounts of the gouvernement du Québec, Secrétariat du Conseil du trésor and ministère des Finances.

3 Investments by school boards, colleges, universities and health and social services institutions include the share paid by the government and that paid by the institutions themselves. It should be noted that the share paid by the government is financed by subsidies for debt service.
Sources: Secrétariat du Conseil du trésor and ministère des Finances.

4 Investments by Hydro-Québec are shown on a calendar-year basis. They exclude financial investments and commercial programs.
Sources: Hydro-Québec and ministère des Finances.

5 Investments by government enterprises correspond to the increase in long-term assets. They exclude investments by consolidated organizations and the Société québécoise d'assainissement des eaux, which are included under "Government" and "Municipalities and municipal bodies" respectively.
Sources: Financial statements of the enterprises of the gouvernement du Québec and ministère des Finances.

6 Investments by municipalities and municipal bodies also include those related to water purification, public transportation and cultural and community facilities.
Sources: Secrétariat du Conseil du trésor, ministère des Affaires municipales, du Sport et du Loisir and ministère des Finances.

The following table presents a comparative analysis of borrowings and investments by the public sector as a whole. Total net public sector borrowings include the change in the net retirement plans liability.

In 2003-2004, total net public sector borrowings are once again lower than investments. The ratio of net borrowings to investments is 0.48.

TABLE 2.16

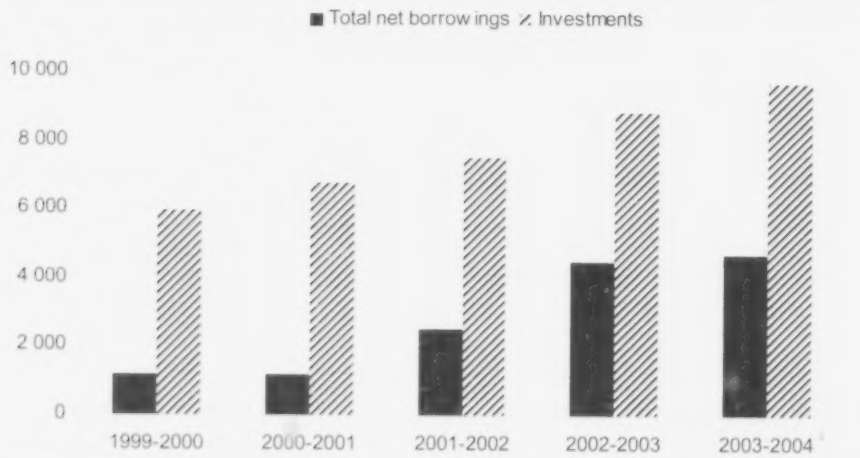
TOTAL NET BORROWINGS AND INVESTMENTS BY THE PUBLIC SECTOR
(millions of dollars)

	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004[1]
Net long-term borrowings[2]	2 255	1 381	3 564	4 125	4 828
Change in the net retirement plans liability[3]	– 1 091	– 226	– 1 051	366	– 143
Total net borrowings	**1 164**	**1 155**	**2 513**	**4 491**	**4 685**
Investments	**5 938**	**6 737**	**7 498**	**8 819**	**9 704**
Ratio	**0.20**	**0.17**	**0.34**	**0.51**	**0.48**

1 Preliminary results.
2 Adjusted by pre-financing.
3 This amount takes into account deposits made in the retirement plans sinking fund and the income of this fund.

GRAPH 2.7

TOTAL NET BORROWINGS[1] AND INVESTMENTS BY THE PUBLIC SECTOR
(millions of dollars)



1 Adjusted by pre-financing.
2 Preliminary results.

Long-term public sector debt

Long-term public sector debt includes the government's total debt as well as the debts of the networks, Hydro-Québec, the municipalities and other government enterprises. In many cases, this debt has served to finance public infrastructure, such as roads, schools, hospitals, hydroelectric dams and water purification plants.

Preliminary results show that the public sector debt should be $181 764 million as at March 31, 2004.

TABLE 2.17

LONG-TERM PUBLIC SECTOR DEBT[1]
(millions of dollars)

	As at March 31				
	2000	**2001**	**2002**	**2003**	**2004**[2]
Total government debt[3, 4]	102 120	104 848	107 175	111 387	114 798
Health and social services and education networks	7 645	8 787	9 588	11 008	10 885
Hydro-Québec	38 135	38 979	37 893	35 639	34 776
Other government enterprises	4 445	4 345	3 906	3 955	3 535
Municipalities and municipal bodies[5]	17 211	16 699	16 777	16 530	17 770
Total	**169 556**	**173 658**	**175 339**	**178 519**	**181 764**

1 Including Treasury bills outstanding of the Consolidated Revenue Fund and the Financing Fund. As at March 31, 2004, Treasury bills outstanding should amount to $2 111 million for the Consolidated Revenue Fund and $1 197 million for the Financing Fund. The Treasury bills of the Financing Fund are used to meet the long-term financing needs of consolidated organizations, the Société québécoise d'assainissement des eaux and certain government enterprises.

2 Preliminary results.

3 Consolidated direct debt and net retirement plans liability, excluding pre-financing totalling $506 million in 1999-2000, $1 475 million in 2000-2001, $1 154 million in 2001-2002, $3 967 million in 2002-2003 and $1 644 million in 2003-2004. These borrowings are allocated to the years to which they apply.

4 Including temporary borrowings used to meet long-term financing needs.

5 Includes the long-term debt of the Société québécoise d'assainissement des eaux.

Historical data and preliminary results

TABLE 2.18

GOUVERNEMENT DU QUÉBEC
SUMMARY OF CONSOLIDATED FINANCIAL TRANSACTIONS
(millions of dollars)

	2000-2001	2001-2002	2002-2003	2003-2004 [1]
Budgetary transactions of Consolidated Revenue Fund[2]				
Own-source revenue before exceptional losses of SGF	40 921	39 023	41 197	42 824
Federal transfers	7 895	8 885	8 932	9 377
Total revenue	48 816	47 908	50 129	52 201
Program spending	- 40 751	- 42 380	- 44 316	- 45 800
Debt service	- 6 972	- 6 687	- 6 536	- 6 668
Total expenditure	- 47 723	- 49 067	- 50 852	- 52 468
Net results of consolidated organizations[2]	284	322	368	267
Budgetary reserve				
Funds allocated to reserve	- 950	—	—	—
Use of funds allocated to reserve	—	950	—	—
Consolidated budget balance before exceptional losses of SGF	**427**	**113**	**- 355**	**0**
Exceptional losses of SGF	—	- 91	- 339	- 364
Consolidated budget balance	**427**	**22**	**- 694**	**- 364**
Consolidated non-budgetary transactions				
Investments, loans and advances	- 1 632	- 1 142	- 1 649	- 1 077
Capital expenditures	- 473	- 995	- 1 482	- 978
Retirement plans	1 793	2 089	2 007	2 221
Other accounts	- 631	- 589	240	- 1 235
Consolidated non-budgetary requirements	**- 943**	**- 637**	**- 884**	**- 1 069**
Consolidated net financial requirements	**- 516**	**- 615**	**- 1 578**	**- 1 433**
Consolidated financing transactions				
Change in cash position[3]	- 1 006	236	- 3 090	2 466
Change in direct debt[3]	3 541	3 519	6 309	1 331
Retirement plans sinking fund[4]	- 2 019	- 3 140	- 1 641	- 2 364
Total financing of consolidated transactions	**516**	**615**	**1 578**	**1 433**

Note: A negative entry indicates a financial requirement and a positive entry, a source of financing. For the change in cash position, a negative entry indicates an increase and a positive entry, a decrease. For purposes of comparison, the data are presented on the basis of the 2004-2005 budgetary structure. Because of the changes that will be made in the family policy as of January 1, 2005, amounts previously found under program spending will be recorded as revenue. The data presented in this table incorporate a restatement that covers a three-month period and that reduces own-source revenue and program spending by $132 million for each fiscal year, without changing the budget balance.

1 Preliminary results.

2 The budgetary transactions of the Consolidated Revenue Fund, which include the profits of government enterprises, are presented separately from those of consolidated organizations. In addition, the budgetary transactions of consolidated organizations are grouped under the new heading "net results of consolidated organizations".

3 The change in direct debt includes new long-term borrowings less repayment of long-term borrowings and the change in temporary borrowings outstanding. Previously, the change in temporary borrowings outstanding was included in the change in cash position. See the explanation of consolidated financing transactions given earlier.

4 This sinking fund receives amounts to be used to cover retirement benefits payable by the government under the public and parapublic sector retirement plans. The investment income of this fund is reinvested in it.

TABLE 2.19

GOUVERNEMENT DU QUÉBEC – CONSOLIDATED REVENUE FUND
REVENUE BY SOURCE BEFORE THE EXCEPTIONAL LOSSES OF THE SGF
(millions of dollars)

	2000-2001	2001-2002	2002-2003	2003-2004 [1]
Own-source revenue				
Income and property taxes				
Personal income tax	16 984	15 791	16 048	16 454
Contributions to Health Services Fund	4 488	4 291	4 068	4 658
Corporate taxes[2]	4 217	4 029	3 735	3 837
	25 689	24 111	23 851	24 949
Consumption taxes				
Sales	7 374	7 557	8 331	9 003
Fuel	1 536	1 536	1 645	1 670
Tobacco	483	652	867	923
	9 393	9 745	10 843	11 596
Duties and permits				
Motor vehicles	646	662	690	700
Alcoholic beverages	146	140	155	156
Natural resources	265	188	201	124
Other	180	177	178	171
	1 237	1 167	1 224	1 151
Miscellaneous				
Sales of goods and services	406	412	440	434
Interest	390	395	321	332
Fines, forfeitures and recoveries	310	371	417	389
	1 106	1 178	1 178	1 155
Revenue from government enterprises before exceptional losses of SGF				
Société des alcools du Québec	471	489	540	563
Loto-Québec	1 358	1 352	1 353	1 393
Hydro-Québec	1 160	1 041	1 840	2 026
Other	507	- 60	368	- 9
	3 496	2 822	4 101	3 973
Total own-source revenue before exceptional losses of SGF	**40 921**	**39 023**	**41 197**	**42 824**
Federal transfers				
Equalization	5 650	5 336	5 315	4 065
Canada Health and Social Transfer	1 597	2 958	2 648	4 266
Other transfers related to fiscal arrangements	30	27	34	64
Other programs	618	564	935	982
Total federal transfers	**7 895**	**8 885**	**8 932**	**9 377**
Total revenue before exceptional losses of SGF	**48 816**	**47 908**	**50 129**	**52 201**

Note: Data restated according to the information provided at the bottom of Table 2.18.
1 Preliminary results.
2 Includes tax on corporate profits, tax on capital and tax on insurance company premiums, as well as tax on telecommunications, gas and electricity.

TABLEAU 2.20

GOUVERNEMENT DU QUÉBEC – CONSOLIDATED REVENUE FUND
EXPENDITURE BY DEPARTMENT
(millions of dollars)

	2000-2001	2001-2002	2002-2003	2003-2004 [1]
Program spending				
Assemblée nationale	80	88	92	94
Personnes désignées par l'Assemblée nationale	42	50	63	97
Affaires municipales, Sport et Loisir	1 388	1 626	1 584	1 575
Agriculture, Pêcheries et Alimentation	714	651	641	664
Conseil du trésor et Administration gouvernementale	446	475	523	488 [2]
Conseil exécutif	79	94	139	168 [2]
Culture et Communications	528	479	490	512
Développement économique et régional et Recherche	1 095	1 008	1 086	798 [2]
Éducation	10 124	10 542	11 099	11 469
Emploi, Solidarité sociale et Famille	5 530	5 636	5 823	5 993
Environnement	155	178	177	180
Finances (excluding debt service)	115	116	127	152 [2]
Justice	468	509	542	573
Relations avec les citoyens et Immigration	185	220	246	210
Relations internationales	104	111	111	112
Ressources naturelles, Faune et Parcs	564	502	506	485
Revenu	715	613	778	642
Santé et Services sociaux	16 095	17 189	17 919	19 105
Sécurité publique	744	799	871	924
Transports	1 501	1 406	1 429	1 488
Travail	79	88	70	69
Total program spending	**40 751**	**42 380**	**44 316**	**45 800**
Debt service				
Direct debt service	4 378	3 970	3 888	3 926
Interest on retirement plans	2 594	2 717	2 648	2 742
Total debt service	**6 972**	**6 687**	**6 536**	**6 668**
Total expenditure	**47 723**	**49 067**	**50 852**	**52 468**

Note: Data restated according to the information provided at the bottom of Table 2.18. In addition, since the data are rounded off, the sum of the amounts recorded for each department may not correspond to the total.

1 Preliminary results.

2 These amounts contain provisions that allow appropriations to be transferred to other departments between the date the Budget documents are produced and the end of the fiscal year.

TABLE 2.21

GOUVERNEMENT DU QUÉBEC
CONSOLIDATED NON-BUDGETARY TRANSACTIONS
(millions of dollars)

	2000-2001	2001-2002	2002-2003	2003-2004 [1]
Investments, loans and advances				
Consolidated Revenue Fund				
Government enterprises				
Shares and investments				
Société générale de financement du Québec	- 350	- 550	- 200	—
Société Innovatech du Grand Montréal	- 42	- 20	- 50	—
Société Innovatech Québec et Chaudière-Appalaches	- 11	- 29	- 30	- 2
Société Innovatech Sud du Québec	- 6	- 19	- 11	- 1
Société Innovatech Régions ressources	- 13	- 12	- 8	- 9
Other	- 3	- 18	- 41	—
	- 425	- 648	- 340	- 12
Change in the equity value of investments	- 1 157	- 371	- 1 138	- 587
Loans and advances	—	—	—	- 5
Total government enterprises	- 1 582	- 1 019	- 1 478	- 604
Individuals, corporations and others	- 20	- 173	- 45	- 211
Municipalities and municipal bodies	1	4	2	2
	- 1 601	- 1 188	- 1 521	- 813
Consolidated organizations	- 31	46	- 128	- 264
Total investments, loans and advances	**- 1 632**	**- 1 142**	**- 1 649**	**- 1 077**
Capital expenditures				
Consolidated Revenue Fund				
Net investments	- 144	- 135	- 200	- 334
Amortization	334	193	207	212
	190	58	7	- 122
Consolidated organizations	- 663	- 1 053	- 1 489	- 856
Total capital expenditures	**- 473**	**- 995**	**- 1 482**	**- 978**

1 Preliminary results.

TABLE 2.21 (CONT.)

GOUVERNEMENT DU QUÉBEC
CONSOLIDATED NON-BUDGETARY TRANSACTIONS
(millions of dollars)

	2000-2001	2001-2002	2002-2003	2003-2004 [1]
Retirement plans				
Contributions by the government as employer				
RREGOP and PPMP				
Cost of credited service[2]	990	1 014	1 053	1 068
Amortization of actuarial gain (-) or loss	66	141	155	153
Other plans				
Cost of credited service[2]	166	147	170	161
Amortization of actuarial gain (-) or loss	26	65	70	73
Cost of changes	—	28	3	—
Total government contribution	1 248	1 395	1 451	1 455
Contributions by independent employers	—	4	4	5
Participants' contributions	106	88	76	200
Total contributions	106	92	80	205
Benefits, repayments and administrative expenses	- 2 567	- 2 720	- 2 913	- 3 043
Interest on actuarial obligation	3 006	3 322	3 389	3 604
Total retirement plans	**1 793**	**2 089**	**2 007**	**2 221**
Other accounts				
Consolidated Revenue Fund	- 490	- 652	244	- 855
Consolidated organizations	- 141	63	- 4	- 380
Total other accounts	**- 631**	**- 589**	**240**	**- 1 235**
Total consolidated non-budgetary transactions	**- 943**	**- 637**	**- 884**	**- 1 069**

Note: A negative entry indicates a financial requirement and a positive entry, a source of financing.
1 Preliminary results.
2 Actuarial value of retirement benefits vested during the fiscal year, calculated according to the actuarial projected benefit method prorated on service.

TABLE 2.22

GOUVERNEMENT DU QUÉBEC
CONSOLIDATED FINANCING TRANSACTIONS
(millions of dollars)

	2000-2001	2001-2002	2002-2003	2003-2004 [1]
Change in cash position				
Consolidated Revenue Fund	- 969	323	- 2 978	2 466
Consolidated organizations	- 37	- 87	- 112	—
Total change in cash position	**- 1 006**	**236**	**- 3 090**	**2 466**
Change in direct debt				
Consolidated Revenue Fund				
New borrowings	7 569	7 700	8 862	4 940
Repayment of borrowings	- 4 616	- 4 890	- 3 943	- 4 842
	2 953	2 810	4 919	98
Consolidated organizations				
New borrowings	1 558	1 311	2 568	2 415
Repayment of borrowings	- 970	- 602	- 1 178	- 1 182
	588	709	1 390	1 233
Total change in direct debt	**3 541**	**3 519**	**6 309**	**1 331**
Retirement plans sinking fund [2]	**- 2 019**	**- 3 140**	**- 1 641**	**- 2 364**
Total financing of consolidated transactions	**516**	**615**	**1 578**	**1 433**

Note: A negative entry indicates a financial requirement and a positive entry, a source of financing. For the change in cash position, a negative entry indicates an increase and a positive entry, a decrease.

1 Preliminary results.

2 This sinking fund receives amounts to be used to cover retirement benefits payable by the government under the public and parapublic sector retirement plans. The investment income of this fund is reinvested in it and applied against the interest on the actuarial obligation to obtain the interest charge on the retirement plans.

TABLE 2.23

GOUVERNEMENT DU QUÉBEC
BORROWINGS FOR THE CONSOLIDATED REVENUE FUND IN 2003-2004

Amount in Canadian dollars[1]	Face value in foreign currency	Interest rate[2]	Date of issue	Date of maturity	Price to investor	Yield to investor[3]
	(millions)	%			$	%
503	—	5.75	July 28	2036-12-01	100.555	5.712
504	—	5.75	December 1	2036-12-01	100.710	5.702
209	AUS$200	6.00	February 18	2009-02-18	100.000	6.000
468	—	5.25	March 11	2013-10-01	105.089	4.586
1 585[4]	—	Various	Various	Various	Various	Various
656[5]	—	Various	Various	Various	Various	Various
793[6]	—	Various	Various	Various	Various	Various
5[7]	—	Various	Various	Various	Various	Various
450[8]	—	Various	Various	Various	Various	Various
– 233[9]	Various	Various	Various	Various	Various	Various
4 940						

1 Borrowings in foreign currency given in Canadian equivalent of their value on the date of borrowing.
2 Interest payable semi-annually except if another frequency is indicated in a note.
3 Yield to investor is determined on the basis of interest payable semi-annually.
4 Medium-term notes on the Canadian market.
5 Real return bonds. The principal and the interest rate of these bonds are adjusted according to the change in the Consumer Price Index in Canada.
6 Savings products issued by Épargne Placements Québec.
7 Borrowings from the Canada Pension Plan Investment Fund.
8 Immigrant Investor Program.
9 Amount received (disbursed) under interest rate and currency swap agreements.

Note: The Québec government has credit agreements with various banks and financial institutions for a total of US$3 500 million. None of these credit agreements is being drawn upon.

TABLE 2.24

GOUVERNEMENT DU QUÉBEC
BORROWINGS FOR THE FINANCING FUND IN 2003-2004

	Amount in Canadian dollars[1]	Face value in foreign currency	Interest rate[2]	Date of issue	Date of maturity	Price to investor	Yield to investor[3]
		(millions)	%			$	%
A. Borrowings for consolidated organizations							
	498[4]	—	4.25[5]	July 9	2010-07-09	99.530	4.329
	502	—	5.25	July 21	2013-10-01	100.423	5.195
	65[6]	—	6.25	September 4	2010-12-01	107.903	4.937
	60[6]	—	5.25	September 4	2013-10-01	99.872	5.266
	504	—	5.25	September 15	2013-10-01	100.782	5.149
	50[6]	—	6.25	November 4	2032-06-01	105.071	5.881
	503	—	5.25	November 20	2013-10-01	100.690	5.159
	77[6]	—	5.25	December 10	2013-10-01	100.625	5.167
	16[6]	—	5.25	December 19	2013-10-01	101.367	5.070
	57	—	5.25	March 11	2013-10-01	105.089	4.586
Sub-total	**2 332**						
B. Borrowings for certain government enterprises							
	85[6]	—	6.25	September 4	2032-06-01	105.407	5.858
	83[6]	—	5.25	December 12	2036-12-01	100.071	5.745
Sub-total	**168**						
Total	**2 500**						

1 Borrowings in foreign currency given in Canadian equivalent of their value on the date of borrowing.
2 Interest payable semi-annually except if another frequency is indicated in a note.
3 Yield to investor is determined on the basis of interest payable semi-annually.
4 Medium-term notes on the European market.
5 Interest payable annually.
6 Borrowings fully subscribed by the Caisse de dépôt et placement du Québec.

TABLE 2.25

GOUVERNEMENT DU QUÉBEC
BORROWINGS BY FINANCEMENT-QUÉBEC IN 2003-2004

Amount in Canadian dollars[1]	Face value in foreign currency	Interest rate[2]	Date of issue	Date of maturity	Price to investor	Yield to investor[3]
(millions)		%			$	%
500[4]	—	Variable[5]	July 4	2007-07-04	100.000	Variable
501	—	4.75	October 21	2009-12-01	100.237	4.704
507	—	4.75	January 9	2009-12-01	101.401	4.476
1 508						

1 Borrowings in foreign currency given in Canadian equivalent of their value on the date of borrowing.
2 Interest payable semi-annually except if another frequency is indicated in a note.
3 Yield to investor is determined on the basis of interest payable semi-annually.
4 Medium-term notes on the Canadian market.
5 Interest payable quarterly.

TABLE 2.26

GOUVERNEMENT DU QUÉBEC
BORROWINGS BY HYDRO-QUÉBEC IN 2003[1]

Amount in Canadian dollars[2]	Face value in foreign currency	Interest rate[3]	Date of issue	Date of maturity	Price to investor	Yield to investor[4]
(millions)		%			$	%
2 249[5]	Various	Various	Various	Various	Various	Various
334[6]	Various	Various	Various	Various	Various	Various
2 583						

1 Borrowings contracted as at December 31, 2003.
2 Borrowings in foreign currency given in Canadian equivalent of their value on the date of borrowing.
3 Interest payable semi-annually except if another frequency is indicated in a note.
4 Yield to investor is determined on the basis of interest payable semi-annually.
5 Medium-term notes on the Canadian market.
6 Amount received under interest rate and currency swap agreements.
Note: Hydro-Québec has credit agreements with various banks and financial institutions for a total of US$1 500 million. None of the credit agreements was being drawn upon at December 31, 2003.

Section 2 Appendix 2.1

Consolidated budgetary transactions: revenue by source and expenditure by mission in 2003-2004

TABLE 2.1.1

GOUVERNEMENT DU QUÉBEC
CONSOLIDATED BUDGETARY TRANSACTIONS: REVENUE BY SOURCE AND EXPENDITURE BY MISSION IN 2003-2004
(millions of dollars)

	Consolidated results			Preliminary results
	Budget Speech of June 12, 2003	Consolidated Revenue Fund	Consolidated organizations	Consolidated results
Revenue by source				
Income and property taxes	25 915	24 949	475	25 424
Consumption taxes	11 715	11 596	140	11 736
Duties and permits	1 318	1 151	132	1 283
Miscellaneous	2 475	1 155	1 447	2 602
Revenue from government enterprises before exceptional losses of SGF	3 942	3 973	—	3 973
Own-source revenue before exceptional losses of SGF	45 365			45 018
Federal transfers	9 584	9 377	498	9 875
Total revenue before exceptional losses of SGF	54 949			54 893
Expenditure by mission				
Health and Social Services	– 19 734	– 19 105	– 662	– 19 767
Education and Culture	– 12 220	– 12 162	– 53	– 12 215
Economy and Environment	– 6 014	– 5 608	– 604	– 6 212
Support for Individuals and Families	– 5 164	– 5 240	– 73	– 5 313
Administration and Justice	– 4 305	– 3 685	– 437	– 4 122
Program spending	– 47 437[1]			– 47 629
Debt service	– 7 512	– 6 668	– 596	– 7 264
Total expenditure	– 54 949			– 54 893
Consolidated budget balance before exceptional losses of SGF	0			0
Exceptional losses of SGF	—			– 364
Consolidated budget balance	0			**– 364**

Note: This purpose of this table, which presents revenue by source and expenditure by mission for fiscal 2003-2004, is to provide better reconciliation with the *consolidated statement of operating results* as it should be presented in the government's financial statements for that fiscal year.

1. The breakdown of expenditure by mission is the same as that which prevailed at the time of the June 12, 2003 Budget Speech.

Section 3

Factors underlying the current budgetary difficulties

Introduction 3

Costly commitments 4

A less favourable economic situation than in the late 1990s 7

Stagnation of federal transfers 10

Introduction

A balanced budget is always fragile, because of the structural problems affecting public finances.

— Québec spends more than the other Canadian provinces despite its lower per capita wealth.

— The tax burden of Quebecers is the heaviest in Canada.

— Québec's debt is the largest of the Canadian provinces.

Special conditions facilitated the achievement of a zero deficit from 1998-1999 to 2002-2003—in particular strong growth in own-source revenue as a result of very favourable economic conditions, the inclusion of large CSST profits in government revenue and the receipt of large one-time payments from the federal government.

The non-recurring nature of these factors, coupled with the costly commitments made by the previous government, make it difficult to achieve a zero deficit now.

Costly commitments

The exceptional economic conditions of the late 1990s made it possible not only to achieve and maintain a balanced budget, but also to implement costly initiatives that the government must defray today and in the years to come. These initiatives include investment and business support measures, and the Public-Sector Investment Acceleration Plan announced in the Budget tabled further to the events of September 11, 2001.

From 1997-1998 to 2002-2003, initiatives totalling more than $13.1 billion were implemented, resulting in commitments of $10.9 billion to be assumed in 2003-2004 and the years to come.

TABLE 3.1

IMPACT OF THE COMMITMENTS MADE BY THE PREVIOUS GOVERNMENT FROM 1997-1998 TO 2002-2003
(millions of dollars)

	1997-1998 to 2002-2003	2003-2004	2004-2005	2005-2006	Subsequent years	Total as of 2003-2004	Years as a whole
Investment and business support							
- FAIRE program	967	122	128	125	1 186	1 561	2 528
- Fiscal measures – designated sites and major projects	486	396	446	440	2 680	3 962	4 448
- Investment losses:[1]							
SGF	433	364	85	21	—	470	903[2]
Innovatech corporations	168	60	11	—	—	71	239
Public-Sector Investment Acceleration Plan[3]	141	140	223	247	4 209	4 819	4 960
Total	**2 195**	**1 082**	**893**	**833**	**8 075**	**10 883**	**13 078**

1 Investments in these government corporations totalled $1.7 billion for the period from 1998 to 2003, including $1.3 billion in the Société générale de financement (SGF) and $400 million in the Innovatech corporations.

2 This amount corresponds to the losses sustained from 2001-2002 to 2003-2004 ($797 million), plus anticipated losses of $106 million in 2004-2005 and 2005-2006.

3 The Public-Sector Investment Acceleration Plan gave rise to investments of $3 billion, including $2.5 billion by government departments and $500 million by government corporations.

Investment and business support

The FAIRE program, which was originally to have been a $250-million temporary intervention program, will ultimately cost $2.5 billion:

— Almost $1 billion in spending was carried out before March 31, 2003.

— Another $1.6 billion in commitments must be defrayed in 2003-2004 and the years to come.

The combined cost of the fiscal measures relating to designated sites (E-Commerce Place, the Cité du multimédia, etc.) and the 10-year tax holiday for major investment projects will total nearly $4.5 billion over 10 years:

— Total costs of $486 million were incurred before March 31, 2003.

— Close to another $4 billion must be assumed in 2003-2004 and the years to come.

Investments in the Société générale de financement (SGF) and the Innovatech corporations from 1998 to 2003 totalled $1.7 billion. These investments did not yield the anticipated results. A total of $1 025 million—60% of the investments made—had to be entered as losses in the government's books from 1997-1998 to 2003-2004.

Public-Sector Investment Acceleration Plan

The Public-Sector Investment Acceleration Plan (PIAP) announced in November 2001 at the time of the 2002-2003 Budget Speech gave rise to investments of over $3 billion. These investments led to $4.8 billion in spending, which will have to be accounted for in 2003-2004 and the years to come (up to 25 years) in order to repay capital and interest.

A spending growth dynamic that was not rectified

The costly initiatives implemented during the period from 1998-1999 to 2002-2003 contributed to a sharp increase in spending, with program spending growth averaging out to 4.6% during those years.

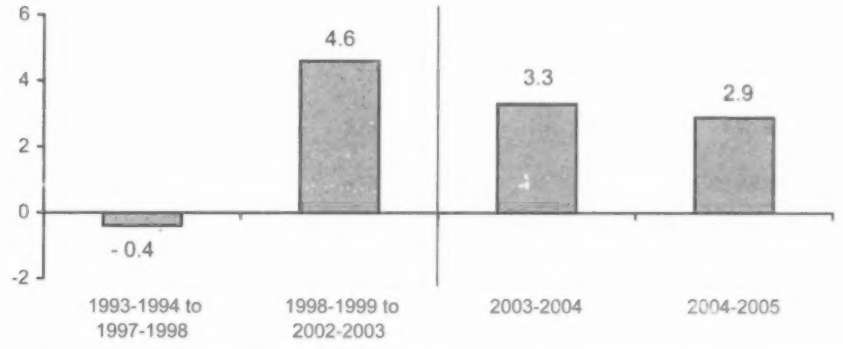
That high growth rate was also due to the introduction of new programs that expanded rapidly (child-care services, prescription drug insurance, etc.). In addition to these factors, there was no systematic review of existing programs.

In comparison, during the five years prior to attaining a zero deficit—that is, from 1993-1994 to 1997-1998—government spending fell an average of 0.4% annually.

For 2003-2004 and 2004-2005, program spending growth was reduced to 3.3% and 2.9% respectively.

CHART 3.1

ANNUAL GROWTH IN PROGRAM SPENDING
(percent)



Source: Secrétariat du Conseil du trésor.

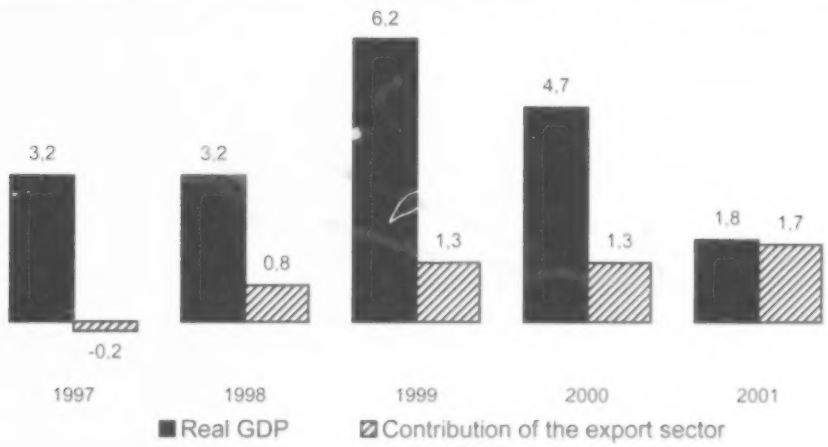
A less favourable economic situation than in the late 1990s

The highly favourable economic conditions of the late 1990s played a major role in balancing the budget. Between 1997 and 2000, real GDP growth in Québec averaged 4.3%, eclipsing the 2.5% rate that had been the average since the early 1980s.

The robust growth in the Québec economy during that period was primarily attributable to the strength of exports to the United States, spurred by sharp growth in the U.S. economy, a weak Canadian dollar compared with the U.S. dollar and high demand for products in fields, such as aeronautics and capital goods, where Québec is a major producer. The export sector contributed almost 1% a year to GDP growth during that period.

CHART 3.2

THE EXPORT SECTOR INCREASED GROWTH BY NEARLY 1%
(percentage change)



Source: Institut de la statistique du Québec.

The vibrancy of the economy in the late 1990s was also due to the positive impact of exceptional stock market returns and low interest rates on household consumption and business investments. It should be noted that present interest rates are the lowest since the early 1960s.

CHART 3.3

SIGNIFICANT DEPRECIATION OF THE CANADIAN DOLLAR IN THE 1990s
(U.S. cents)

Sources: Bank of Canada and ministère des Finances du Québec.

CHART 3.4

LOWEST INTEREST RATES IN 40 YEARS
(overnight financing rate, percent)

Sources: Bank of Canada and ministère des Finances du Québec.

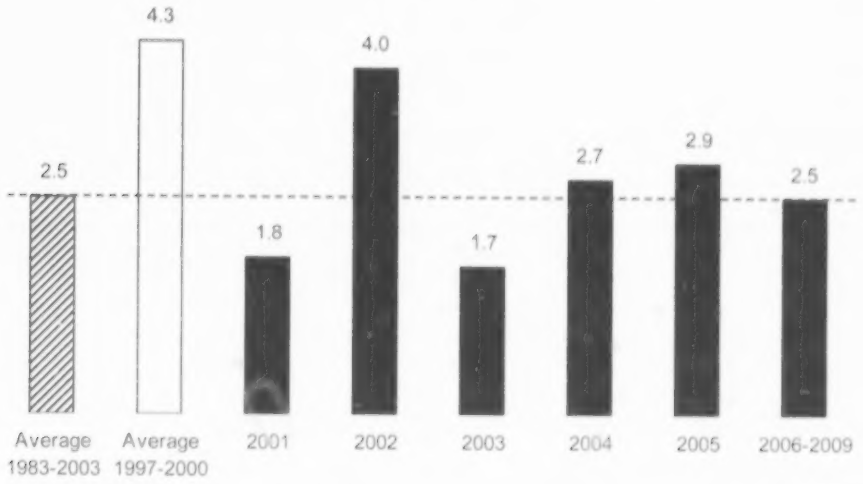
These developments brought about a significant increase in government revenue and substantial debt service savings. That leeway enabled the government to reduce taxes and maintain high spending growth without jeopardizing its balanced budget.

However, that manoeuvring room will likely disappear by the end of this decade, as economic expansion should be more moderate, averaging roughly 2.5%, the pace of the last two decades.

The factors that allowed for such rapid economic growth in the late 1990s will play a less prominent role in the coming years.

CHART 3.5

ECONOMIC OUTLOOK FOR QUÉBEC
(GDP, constant dollars, average annual percentage change)



Sources: Institut de la statistique du Québec and ministère des Finances du Québec.

High U.S. demand for Québec products, particularly capital goods, in the late 1990s generated an exceptional increase in Québec exports, which rose 11.4% annually from 1997 to 2000. However, in 2001, the recession in the United States gave rise to a large excess productive capacity which, in turn, caused a considerable drop in foreign demand for Québec products and a decline in exports over the next three years.

The anticipated moderate growth in the U.S. economy until 2009 should result in an increase in Québec exports expected to average out to 5% annually from 2004 to 2009. However, in the short term, the strength of the Canadian dollar and the under-used productive capacity in certain sectors, such as aeronautics and new technologies, in the United States will slow the expansion of Québec exports.

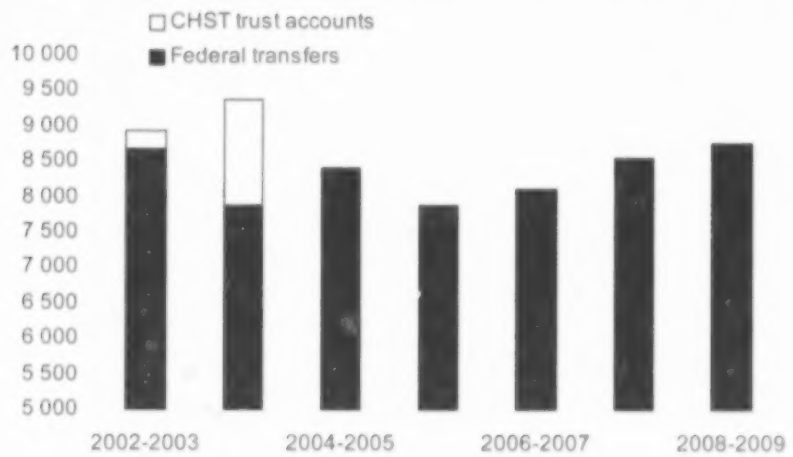
Moreover, current interest rates, which are the lowest in over 40 years, can only rise with the recovery of the North American economy. As a result, growth in domestic demand, particularly in the business investment sector, will be limited to 4% in the coming years, whereas it rose more than 10% from 1997 to 2000.

Stagnation of federal transfers

The final factor making it harder to balance the budget now is the stagnation of federal transfer revenue, compared with the level in 2003-2004, for the entire forecast horizon. This situation differs from that of the late 1990s and early stages of the present decade, when additional health transfers, notably through non-recurring trust accounts, were granted by the federal government.

CHART 3.6

CHANGE IN FEDERAL TRANSFER REVENUE
(excluding consolidated organizations, in millions of dollars)



Sources: Ministère des Finances du Canada and ministère des Finances du Québec.

Two phenomena are primarily responsible for the anticipated stagnation of federal transfer revenue. The Québec economy is expected to continue to perform well compared with the other Canadian provinces, so equalization revenue for that period will not exceed that received in 2002-2003.

However, the stagnation of federal transfers to Québec points especially to the federal government's refusal to redress the major weaknesses of the equalization program and ensure adequate health-care funding.

The equalization program, as it is currently structured, maintains significant fiscal disparities between the provinces, in particular because of the inadequate definition of the standard of the program, the shortcomings of the measure of fiscal capacity for property taxes and the incomplete coverage of provincial revenues, particularly regarding user fees. The program changes proposed by the federal government do not correct these major weaknesses.

Moreover, the federal contribution of only 16 cents per dollar of provincial health spending is woefully insufficient, considering the federal government's initial promise to cover 50% of health-care costs, the size of federal surpluses and the priority that Quebecers and Canadians place on health care. The paper *Correcting Fiscal Imbalance* discusses these problems in detail.

Section 4

The Government's Budgetary and Financial Stance

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A balanced budget maintained 4

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The government devotes a shrinking proportion of its revenue to interest on the debt 17
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Appendix

4.1 Additional information on the government's financial position 19

Introduction

The budgetary and financial stance of the government is presented in this section of the Budget Plan.

The information provided includes:

— the result of forecasts made for 2004-2005 and 2005-2006, once the impact of the fiscal and budgetary measures announced in the present Budget is incorporated;

— brief explanations of the anticipated change in revenue and expenditure;

— a glimpse of the change in the main financial indicators.

A balanced budget maintained

In accordance with the objectives of the government, a balanced budget was maintained in 2003-2004, prior to consideration of the exceptional loss of the Société générale de financement du Québec (SGF). Taking into account these additional losses, the deficit stands at $364 million.

For 2004-2005, the government will respect its commitment to maintain a balanced budget. Revenue of $880 million will come from the sale of assets and the disposition of investments that have matured or have become less necessary to the proper conduct of operations of government corporations. This operation is in keeping with the government's revision of the role of the state.

For 2005-2006, the government must make up a budgetary shortfall of $1 623 million.

TABLE 4.1

SUMMARY OF CONSOLIDATED FINANCIAL OPERATIONS[1,2,3]
(millions of dollars)

	2002-2003	2003-2004 P	2004-2005 P	2005-2006 P
Budgetary transactions of the Consolidated Revenue Fund				
Own-source revenue before the exceptional losses of the SGF[4]	41 197	42 824	45 358	45 714
Federal transfers	8 932	9 377	8 476	7 876
Total revenue	**50 129**	**52 201**	**53 834**	**53 590**
Program spending	– 44 316	– 45 800	– 47 151	– 48 377
Debt service	– 6 536	– 6 668	– 6 939	– 7 053
Total expenditure	**– 50 852**	**– 52 468**	**– 54 090**	**– 55 430**
Net results of consolidated organizations[5]	368	267	256	217
Consolidated budgetary balance before exceptional losses of the SGF	**– 355**	**0**	**0**	**– 1 623**
Exceptional losses of the SGF	– 339	– 364	—	—
Shortfall to be absorbed	—	—	—	1 623
Consolidated budgetary balance	**– 694**	**– 364**	**0**	**0**
Consolidated non-budgetary requirements	**– 884**	**– 1 069**	**– 464**	**– 244**
Consolidated net financial requirements				
Consolidated Revenue Fund	– 300	– 200	500	750
Consolidated organizations	– 1 278	– 1 233	– 964	– 994
Total	**– 1 578**	**– 1 433**	**– 464**	**– 244**

P: Preliminary results for 2003-2004 and forecasts for subsequent years.
1 A negative entry indicates a financial requirement and a positive entry, a source of financing.
2 Because of the changes made in the family policy as of January 1, 2005, amounts previously found under program spending are entered under revenue. The data presented in the *2004-2005 Budget* incorporate a restatement that covers a three-month period and that reduces revenue and program spending by $132 million. The restatement, which has no impact on the budgetary balance, will be adjusted as of 2005-2006 to cover a full year and will total $528 million, i.e. an additional amount of $396 million.
3 Contrary to previous years, the budgetary transactions of consolidated organizations are distinguished from the budgetary transactions of the Consolidated Revenue Fund and are grouped under the heading "net results of consolidated organizations".
4 Own-source revenue of the Consolidated Revenue Fund includes the net revenue of government enterprises.
5 Detailed information regarding the net results of consolidated organizations is given in Table 4.11.

The net financial surpluses of the Consolidated Revenue Fund will be $500 million in 2004-2005 and $750 million in 2005-2006.

The net financial requirements of consolidated organizations will stand at $964 million in 2004-2005 and $994 million in 2005-2006. These requirements stem mainly from the investments made by the Fonds de conservation et d'amélioration du réseau routier.

Overall, consolidated net financial requirements will total $464 million in 2004-2005 and $244 million in 2005-2006.

Revenue

Budgetary revenue

The government's budgetary revenue should total $53 834 million in 2004-2005, i.e. $45 358 million in own-source revenue and $8 476 million in federal transfers. After recording an increase of 4.1% in 2003-2004, budgetary revenue should rise by 3.1% in 2004-2005 and decrease by 0.5% in 2005-2006.

TABLE 4.2

CONSOLIDATED REVENUE FUND
CHANGE IN REVENUE
(millions of dollars)

	2002-2003	2003-2004[P]	2004-2005[P]	2005-2006[P]
Own-source revenue[1]	41 197	42 824	45 358	45 714
% change	5.8	3.9	5.9	0.8
Federal transfers	8 932	9 377	8 476	7 876
% change	0.5	5.0	– 9.6	– 7.1
Total	**50 129**	**52 201**	**53 834**	**53 590**
% change	4.8	4.1	3.1	– 0.5
Nominal GDP growth rate in %	5.6	5.2	4.3	4.0
Inflation rate in Canada in %	2.2	2.8	1.5	1.7

P Preliminary results for 2003-2004 and forecasts for subsequent years.
1 Before the exceptional losses of $339 million in 2002-2003 and $364 million in 2003-2004 of the Société générale de financement du Québec.

Own-source revenue

In 2003-2004, own-source revenue was to climb by 3.9% compared with the previous year. Excluding the decline of 3.1% in the revenue of government enterprises, own-source revenue increased in 2003-2004 by 4.7%, or slightly less than the increase in the gross domestic product (GDP).

In 2004-2005, own-source revenue should grow by 5.9%, the largest increases being recorded in corporate income taxes, because of the impact of the fiscal measures announced in the 2003-2004 and 2004-2005 budgets, and in government enterprises, considering the additional revenue of $880 million following the sale of some of their assets. The non-recurrence of this revenue and the impact on a fiscal year basis of the reduction in personal income tax will limit growth in own-source revenue to 0.8% in 2005-2006.

TABLE 4.3

CONSOLIDATED REVENUE FUND
CHANGE IN OWN-SOURCE REVENUE BY SOURCE[1]
(millions of dollars)

	2002-2003	2003-2004[P]	2004-2005[P]	2005-2006[P]
Personal income tax	16 048	16 454	17 201	17 660
% change	1.6	2.5	4.5	2.7
Health Services Fund	4 068	4 658	4 869	5 083
% change	– 5.2	14.5	4.5	4.4
Corporate taxes	3 735	3 837	4 248	4 404
% change	– 7.3	2.7	10.7	3.7
Consumption taxes	10 843	11 596	11 899	12 165
% change	11.3	6.9	2.6	2.2
Other revenue	2 402	2 306	2 318	2 314
% change	2.4	– 4.0	0.5	– 0.2
Sub-total	**37 096**	**38 851**	**40 535**	**41 626**
% change	2.5	4.7	4.3	2.7
Government enterprises[1]	4 101	3 973	4 823	4 088
% change	50.2	– 3.1	21.4	– 15.2
Own-source revenue	**41 197**	**42 824**	**45 358**	**45 714**
% change	5.8	3.9	5.9	0.8
Nominal GDP growth rate in %[2]	5.6	5.2	4.3	4.0

P: Preliminary results for 2003-2004 and forecasts for subsequent years.
1 Before the exceptional losses of $339 million in 2002-2003 and $364 million in 2003-2004 of the Société générale de financement du Québec.
2 For the calendar year ending three months before the end of the fiscal year.

More specifically, in regard to the change in revenue by source:

— personal income tax, the main source of government revenue, should increase by 4.5% to total $17.2 billion in 2004-2005. During that fiscal year, the progression in tax revenue stemming from the growth in income subject to tax will be offset in part by the impact of the tax reduction announced in the present Budget. In 2005-2006, the increase in revenue should total 2.7%, an increase compatible with the growth in income subject to tax, without considering the impact of the measures announced in this Budget;

— contributions to the Health Services Fund should rise in 2004-2005 by 4.5%. That growth is comparable to the growth in salaries and wages on a fiscal year basis. This will also be the case in 2005-2006, when growth is expected to be 4.4%;

— growth in anticipated revenue from corporate taxes totalling 10.7% in 2004-2005 and 3.7% in 2005-2006 mainly reflects the growth in company profits and the impact of the measures announced in this Budget as well as the previous one;

— in 2004-2005, revenue from consumption taxes should show an increase of 2.6%. That small variation reflects, first of all, the impact on the growth rate of the improvement made as of 2003-2004 in the method used to consider all remittances related to sales made before March 31. That impact is wholly offset by the effect over a full year of the increase in the tobacco tax, announced last December;

— with regard to government enterprises, revenue should grow by 21.4% in 2004-2005. That growth is mainly attributable to the fact that the government plans to realize revenue of $880 million from the sale of assets or the disposition of investments.

TABLE 4.4

CONSOLIDATED REVENUE FUND
CHANGE IN THE REVENUE OF GOVERNMENT ENTERPRISES[1]
(millions of dollars)

	2002-2003	2003-2004[P]	2004-2005[P]
Hydro-Québec	1 840	2 026	2 040
Loto-Québec	1 353	1 393	1 419
Société des alcools du Québec	540	563	601
Other	368	– 9	763
Total	**4 101**	**3 973**	**4 823**
% change	50.2	– 3.1	21.4

P: Preliminary results for 2003-2004 and forecasts for subsequent years.
1 Before the exceptional losses of $339 million in 2002-2003 and $364 million in 2003-2004 of the Société générale de financement du Québec.

Federal transfers

After rising by 5.0% in 2003-2004, revenue from federal transfers should decline by 9.6% in 2004-2005 and 7.1% 2005-2006.

TABLE 4.5

CONSOLIDATED REVENUE FUND
CHANGE IN FEDERAL TRANSFER REVENUE
(millions of dollars)

	2002-2003	2003-2004[P]	2004-2005[P]	2005-2006[P]
Equalization	5 315	4 065	4 942	3 887
% change	– 0.4	– 23.5	21.6	– 21.3
Canada Health and Social Transfer (CHST)	2 648	4 266	2 890	3 302
% change	– 10.5	61.1	– 32.3	14.3
Other transfers related to fiscal arrangements	34	64	25	25
% change	79.4	88.2	– 60.9	–
Other programs	935	982	619	662
% change	65.8	5.0	– 37.0	6.9
Total federal transfers	**8 932**	**9 377**	**8 476**	**7 876**
% change	0.5	5.0	– 9.6	– 7.1

P Preliminary results for 2003-2004 and forecasts for subsequent years.

The 5.0% growth in federal transfers in 2003-2004 reflects the implementation of a mechanism to defer and spread out part of the downward revisions of equalization and the CHST. The amount deferred totals $1 161 million. Without that mechanism, federal transfers would have dropped by 8.0%.

In 2004-2005, the 9.6% decline in transfers reflects the non-recurrence of the bulk of the federal transfer increases stemming from the February 2003 federal announcement on health care. After generating additional revenue of $1.6 billion in 2003-2004, that announcement will have an impact of only $352 million in 2004-2005. However, the establishment of a refundable equalization floor mechanism will make it possible to defer the reimbursement of $1 142 million. Without that mechanism and the mechanism established for 2003-2004, federal transfers would have fallen by 11.4%.

TABLE 4.6

IMPACT IN QUÉBEC OF THE FEBRUARY 2003 FEDERAL ANNOUNCEMENT ON HEALTH CARE
(millions of dollars)

	2003-2004	2004-2005	2005-2006
Health Reform Fund	**236**	**352**	**816**
Non-recurrent trusts			
CHST supplement of $2.5 billion	587	—	—
Diagnostic/Medical Equipment Fund	352	—	—
CHST supplement of $2 billion	471	—	—
Sub-total	1 410	—	—
Total	**1 646**	**352**	**816**
Change		– 1 294	464

In 2005-2006, federal transfers should fall by 7.1%. The beginning of reimbursements stemming from the mechanisms established in 2003-2004 and 2004-2005 will result in a decline of $472 million in federal transfers. However, that drop will be offset by the positive, although minimal, impact of the proposed renewal of equalization announced in the last federal budget.

Although Québec feels that the federal government proposals do not adequately remedy the principal shortcomings of the equalization program, and it intends to step up its efforts to obtain other improvements in the coming months, the currently proposed reform constitutes the minimum gain it could obtain. That is why this impact has been incorporated into the financial framework.

TABLE 4.7

IMPACT IN QUÉBEC OF THE FEDERAL GOVERNMENT PROPOSALS CONCERNING THE RENEWAL OF EQUALIZATION
(millions of dollars)

	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009
Impact in Québec	**70**	**195**	**368**	**554**	**560**

Source: Department of Finance Canada

Measures to defer and spread out the impact of the reduction in federal transfers

Given the magnitude of the anticipated fall in federal transfer revenue in 2003-2004 and 2004-2005, Québec opened discussions with the federal government in the fall of 2003. The discussions led to the establishment of solutions aimed at deferring part of the reduction in federal transfers for each of the two years. All the provinces can avail themselves of those measures.

In 2003-2004, the updating of population data, between October 2003 and February 2004, following the 2001 census, and data on personal and corporate income tax reduced Québec's equalization and CHST revenue by $1 161 million. The federal government allowed that amount to be deferred and spread over five years beginning in 2005-2006.

In regard to 2004-2005, the federal government established a refundable equalization floor mechanism. Québec's equalization entitlement for 2004-2005 cannot be lower than the average entitlement observed from 1999-2000 to 2002-2003. The difference between the floor and the level of entitlement for 2004-2005 may be spread over five years beginning in 2005-2006. On the basis of the last federal estimates, the application of this mechanism will make it possible to defer a reduction in equalization revenue of $1 142 million in 2004-2005.

Given these measures, federal transfers were increased by a total of $2 361 million in 2003-2004 and 2004-2005 and will be reduced by $472 million over a period of five years as of 2005-2006. Hence, these measures provide the Québec government with no additional leeway in the medium term. In fact, they merely reduce the particularly destabilizing impact on the Québec government's financial framework of erratic fluctuations in federal transfers.

TABLE 4.8

CONSOLIDATED REVENUE FUND
IMPACT OF MEASURES TO DEFER AND SPREAD OUT THE REDUCTIONS IN FEDERAL TRANSFERS
(millions of dollars)

	2002-2003	2003-2004[P]	2004-2005[P]	2005-2006[P]
Transfers before deferral of part of the reductions	**8 932**	**8 216**	**7 276**	**8 348**
% change	0.5	– 8.0	– 11.4	14.7
Deferral and spreading out of reductions for 2003-2004	—	1 161	58[1]	– 244
Refundable floor for 2004-2005	—	—	1 142	– 228
Impact of the measures		**1 161**	**1 200**	**– 472**
Transfers after deferral of part of the reductions	**8 932**	**9 377**	**8 476**	**7 876**
% change	0.5	5.0	– 9.6	– 7.1

P Preliminary results for 2003-2004 and forecasts for subsequent years

1 Because of the CHST payment mechanism, part of the 2003-2004 revisions were already deferred until 2004-2005 in the government's financial framework. The deferral of the 2003-2004 revisions explains the gain of $58 million in 2004-2005

Expenditure

Government expenditure should total $54 090 million in 2004-2005. Program spending will be $47 151 million, whereas debt service will amount to $6 939 million.

Program spending

Program spending will increase by 2.9% in 2004-2005 and 2.6% in 2005-2006.

TABLE 4.9

CONSOLIDATED REVENUE FUND
CHANGE IN EXPENDITURE[1]
(millions of dollars)

	2002-2003	2003-2004[P]	2004-2005[P]	2005-2006[P]
Program spending in the Budget of June 12, 2003	– 44 126	– 45 800	– 45 800	– 45 800
% change	3.8	3.8	—	—
Change in expenditure in 2002-2003[2]	– 190	—	—	—
Growth objective for the coming years				
2004-2005	—	—	– 1 351	– 1 351
2005-2006	—	—	—	– 1 226
Program spending	**– 44 316**	**– 45 800**	**– 47 151**	**– 48 377**
% change	4.3	3.3	2.9	2.6
Debt service	– 6 536	– 6 668	– 6 939	– 7 053
% change	– 2.3	2.0	4.1	1.6
Expenditure	**– 50 852**	**– 52 468**	**– 54 090**	**–55 430**
% change	3.6	3.2	3.1	2.5
Nominal GDP growth rate in %[3]	5.6	5.2	4.3	4.0
Inflation rate in Canada in %	2.2	2.8	1.5	1.7

P Preliminary results for 2003-2004 and forecasts for subsequent years.

1 Because of the changes made in the family policy as of January 1, 2005, amounts previously found under program spending are entered under revenue. The data presented in the *2004-2005 Budget* incorporate a restatement that covers a three-month period and that reduces revenue and program spending by $132 million. The restatement, which has no impact on the budgetary balance, will be adjusted as of 2005-2006 to cover a full year and will total $528 million, i.e. an additional amount of $396 million.

2 Including additional expenditure of $322 million and the restatement of $132 million mentioned in the preceding footnote.

3 For the calendar year ending three months before the end of the fiscal year.

Debt service

Debt service has two components, i.e. direct debt service of the Consolidated Revenue Fund and interest ascribed to the retirement plans.

TABLE 4.10

CONSOLIDATED REVENUE FUND
DEBT SERVICE
(millions of dollars)

	2002-2003	2003-2004[P]	2004-2005[P]	2005-2006[P]
Direct debt service	– 3 888	– 3 926	– 4 131	– 4 291
% change	– 2.1	1.0	5.2	3.9
Interest ascribed to the retirement plans[1]	– 2 648	– 2 742	– 2 808	– 2 762
% change	– 2.5	3.5	2.4	– 1.6
Debt service	– 6 536	– 6 668	– 6 939	– 7 053
% change	– 2.3	2.0	4.1	1.6

P: Preliminary results for 2003-2004 and forecasts for subsequent years.
1 Interest ascribed to the retirement plans is equal to the interest on the actuarial obligation less the investment income of the retirement plans sinking fund.

Debt service should rise from $6 536 million in 2002-2003 to $7 053 million in 2005-2006, an increase of $517 million in three years.

The anticipated increase for 2004-2005 is explained mainly by the reduction in the revenue of the sinking fund for borrowings and the retirement plans sinking fund; that revenue is recorded as a reduction of debt service. In 2005-2006, the anticipated increase in interest rates is the main factor in the growth of debt service.

Consolidated organizations

The consolidated organizations should record net results of $256 million in 2004-2005 and $217 million in 2005-2006. These changes are of little significance compared with the net results recorded in 2003-2004.

TABLE 4.11

CONSOLIDATED ORGANIZATIONS
CHANGE IN BUDGETARY TRANSACTIONS
(millions of dollars)

	2002-2003	2003-2004[P]	2004-2005[P]	2005-2006[P]
Revenue				
Own-source revenue	2 160	2 194	2 395	2 394
Federal transfers	375	498	495	446
	2 535	**2 692**	**2 890**	**2 840**
Expenditure				
Expenditure excluding debt service	– 1 618	– 1 829	– 1 980	– 1 917
Debt service	– 549	– 596	– 654	– 706
	– 2 167	**– 2 425**	**– 2 634**	**– 2 623**
Net results	**368**	**267**	**256**	**217**

P: Preliminary results for 2003-2004 and forecasts for subsequent years.

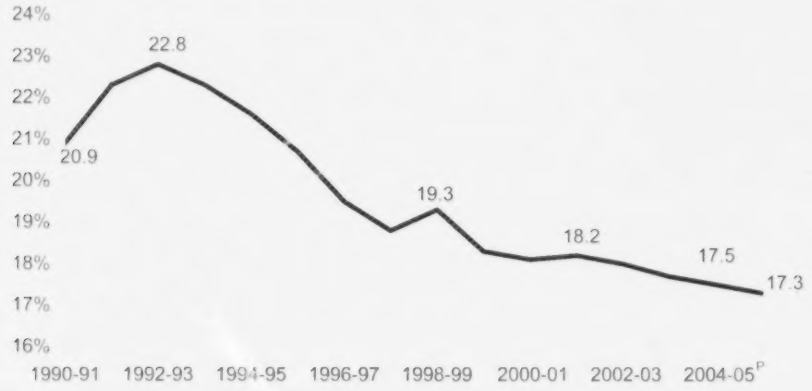
Main financial indicators

Responsible management of spending

The ratio of the government's program spending to GDP should continue to decrease and will reach 17.3% in 2005-2006, the lowest level since the 1970-1971 fiscal year.

GRAPH 4.1

PROGRAM SPENDING
(as a percentage of GDP)



P: Preliminary results for 2003-2004 and forecasts for subsequent years.

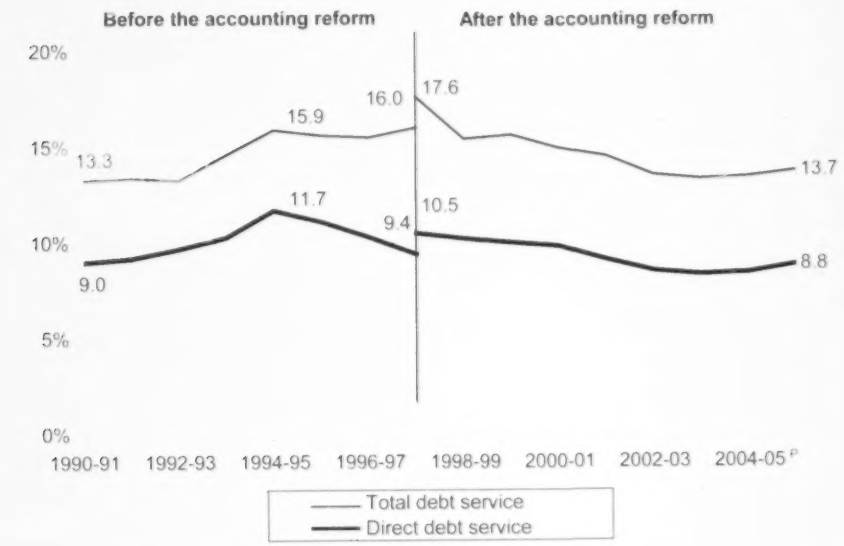
The government devotes a shrinking proportion of its revenue to interest on the debt

The share of budgetary revenue devoted to the direct debt service of the Consolidated Revenue Fund and consolidated organizations will stand at 8.8% in 2005-2006.

As for the share of budgetary revenue devoted to total debt service, which also includes interest ascribed to the retirement plans and the debt service of consolidated organizations, it was 17.6% in 1997-1998, whereas it should reach 13.7% in 2005-2006. Despite an improvement in this ratio, nearly 14 cents for each dollar of income and other taxes collected still cannot be used to provide the public with services.

GRAPH 4.2

DEBT SERVICE
(as a percentage of budgetary revenue)



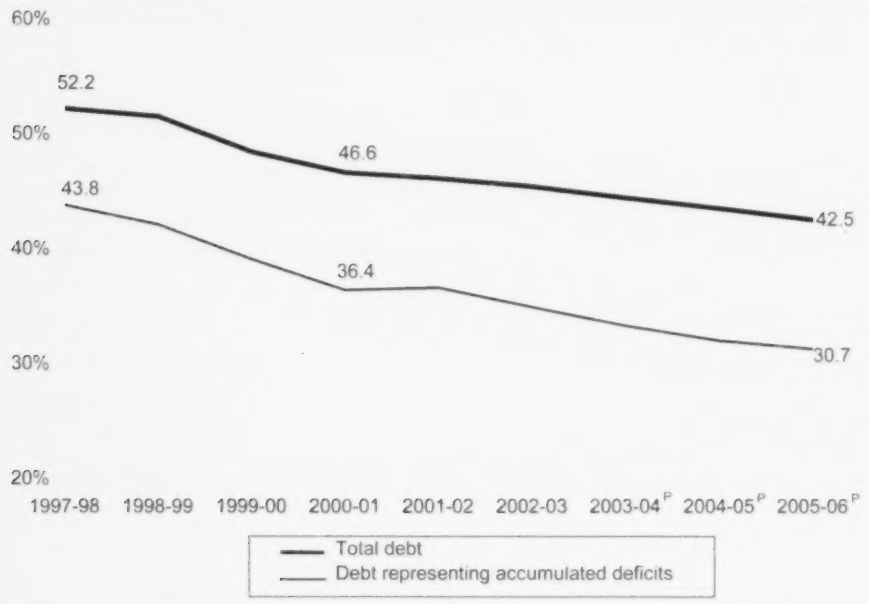
P: Preliminary results for 2003-2004 and forecasts for subsequent years.

An on-going reduction in the rate of indebtedness

The weight of the total debt as a proportion of gross domestic product should drop from 52.2% in 1997-1998 to 42.5% in 2005-2006. The debt representing accumulated deficits has diminished as a proportion of GDP and will stand at 30.7% as at March 31, 2006.

GRAPH 4.3

TOTAL DEBT AND DEBT REPRESENTING ACCUMULATED DEFICITS
(as a percentage of GDP)



P: Preliminary results for 2003-2004 and forecasts for subsequent years.

Section 4 Appendix 4.1

Additional information on the government's financial position

TABLE 4.1.1

CONSOLIDATED REVENUE FUND[1,2] BUDGETARY TRANSACTIONS

(millions of dollars)

	Own-source revenue[3]	Federal transfers	Total revenue	Program spending	Debt service	Total expenditure
Before reform of government accounting						
1970-1971	2 672	1 094	3 766	– 3 714	– 197	– 3 911
1971-1972	3 110	1 293	4 403	– 4 548	– 210	– 4 758
1972-1973	3 672	1 261	4 933	– 5 038	– 242	– 5 280
1973-1974	4 279	1 376	5 655	– 6 026	– 288	– 6 314
1974-1975	5 267	1 871	7 138	– 7 284	– 296	– 7 580
1975-1976	6 001	2 222	8 223	– 8 806	– 368	– 9 174
1976-1977	7 016	2 520	9 536	– 10 256	– 456	– 10 712
1977-1978	7 880	3 088	10 968	– 11 066	– 606	– 11 672
1978-1979	8 403	3 268	11 671	– 12 352	– 817	– 13 169
1979-1980	9 340	3 754	13 094	– 14 524	– 970	– 15 494
1980-1981	10 640	3 894	14 534	– 16 633	– 1 382	– 18 015
1981-1982	13 339	4 473	17 812	– 18 483	– 1 950	– 20 433
1982-1983	14 624	5 172	19 796	– 19 959	– 2 300	– 22 259
1983-1984	15 634	6 227	21 861	– 21 514	– 2 511	– 24 025
1984-1985	16 083	6 236	22 319	– 23 180	– 3 012	– 26 192
1985-1986	17 997	6 178	24 175	– 24 294	– 3 354	– 27 648
1986-1987	19 787	5 828	25 615	– 25 031	– 3 556	– 28 587
1987-1988	22 234	6 117	28 351	– 27 072	– 3 675	– 30 747
1988-1989	23 640	6 386	30 026	– 27 928	– 3 802	– 31 730
1989-1990	24 713	6 674	31 387	– 29 136	– 4 015	– 33 151
1990-1991	26 500	6 972	33 472	– 32 010	– 4 437	– 36 447
1991-1992	28 197	6 747	34 944	– 34 579	– 4 666	– 39 245
1992-1993	28 105	7 764	35 869	– 36 143	– 4 756	– 40 899
1993-1994	28 767	7 762	36 529	– 36 136	– 5 316	– 41 452
1994-1995	29 411	7 494	36 905	– 36 844	– 5 882	– 42 726
1995-1996	30 604	8 126	38 730	– 36 643	– 6 034	– 42 677
1996-1997	31 134	6 704	37 838	– 35 195	– 5 855	– 41 050
After reform of government accounting						
1997-1998	34 363	5 656	40 019	– 35 449	– 6 765	– 42 214
1998-1999	36 837	7 813	44 650	– 37 907	– 6 573	– 44 480
1999-2000	39 094	6 064	45 158	– 38 599	– 6 751	– 45 350
2000-2001	40 921	7 895	48 816	– 40 751	– 6 972	– 47 723
2001-2002	38 932	8 885	47 817	– 42 380	– 6 687	– 49 067
2002-2003	40 858[4]	8 932	49 790[4]	– 44 316	– 6 536	– 50 852
2003-2004[P]	42 460[4]	9 377	51 837[4]	– 45 800	– 6 668	– 52 468

P: Preliminary results.

1 A negative entry indicates a financial requirement and a positive entry, a source of financing.

2 Data for the "Consolidated Revenue Fund" exclude the revenue and expenditure of the consolidated organizations, which appear in Table 4.1.2.

3 Own-source revenue of the Consolidated Revenue Fund includes the net revenue of government enterprises.

4 Own-source revenue includes the exceptional losses of the Société générale de financement du Québec of $339 million in 2002-2003 and $364 million in 2003-2004.

TABLE 4.1.2

CONSOLIDATED ORGANIZATIONS[1]
BUDGETARY TRANSACTIONS
(millions of dollars)

	Own-source revenue	Federal transfers	Total revenue	Expenditure excluding debt service	Debt service	Total expenditure	Net results
1970-1971							
1971-1972							
1972-1973							
1973-1974							
1974-1975							
1975-1976							
1976-1977							
1977-1978							
1978-1979							
1979-1980							
1980-1981							
1981-1982							
1982-1983							
1983-1984							
1984-1985							
1985-1986							
1986-1987							
1987-1988							
1988-1989							
1989-1990							
1990-1991							
1991-1992							
1992-1993							
1993-1994							
1994-1995							
1995-1996							
1996-1997							
After reform of government accounting							
1997-1998	1 391	318	1 709	– 1 094	– 577	– 1 671	38
1998-1999	1 680	258	1 938	– 1 368	– 614	– 1 981	– 44
1999-2000	1 850	270	2 120	– 1 300	– 621	– 1 921	199
2000-2001	1 851	250	2 101	– 1 183	– 634	– 1 817	284
2001-2002	1 940	420	2 360	– 1 464	– 574	– 2 038	322
2002-2003	2 160	375	2 535	– 1 618	– 549	– 2 167	368
2003-2004[P]	2 194	498	2 692	– 1 829	– 596	– 2 425	267

Data not incorporated into the accounting entity

P: Preliminary results.
1 A negative entry indicates a financial requirement and a positive entry, a source of financing.

TABLE 4.1.3

SUMMARY OF CONSOLIDATED FINANCIAL TRANSACTIONS[1]

(millions of dollars)

	Budgetary transactions[2]							
	Own-source revenue	Federal transfers	Total revenue	Expenditure excluding debt service	Debt service	Total expenditure	Budgetary reserve	Surplus (deficit) after reserve
Before reform of government accounting								
1970-1971	2 672	1 094	3 766	– 3 714	– 197	– 3 911		– 145
1971-1972	3 110	1 293	4 403	– 4 548	– 210	– 4 758		– 355
1972-1973	3 672	1 261	4 933	– 5 038	– 242	– 5 280		– 347
1973-1974	4 279	1 376	5 655	– 6 026	– 288	– 6 314		– 659
1974-1975	5 267	1 871	7 138	– 7 284	– 296	– 7 580		– 442
1975-1976	6 001	2 222	8 223	– 8 806	– 368	– 9 174		– 951
1976-1977	7 016	2 520	9 536	– 10 256	– 456	– 10 712		– 1 176
1977-1978	7 880	3 088	10 968	– 11 066	– 606	– 11 672		– 704
1978-1979	8 403	3 268	11 671	– 12 352	– 817	– 13 169		– 1 498
1979-1980	9 340	3 754	13 094	– 14 524	– 970	– 15 494		– 2 400
1980-1981	10 640	3 894	14 534	– 16 633	– 1 382	– 18 015		– 3 481
1981-1982	13 339	4 473	17 812	– 18 483	– 1 950	– 20 433		– 2 621
1982-1983	14 624	5 172	19 796	– 19 959	– 2 300	– 22 259		– 2 463
1983-1984	15 634	6 227	21 861	– 21 514	– 2 511	– 24 025		– 2 164
1984-1985	16 083	6 236	22 319	– 23 180	– 3 012	– 26 192		– 3 873
1985-1986	17 997	6 178	24 175	– 24 294	– 3 354	– 27 648		– 3 473
1986-1987	19 787	5 828	25 615	– 25 031	– 3 556	– 28 587		– 2 972
1987-1988	22 234	6 117	28 351	– 27 072	– 3 675	– 30 747		– 2 396
1988-1989	23 640	6 386	30 026	– 27 928	– 3 802	– 31 730		– 1 704
1989-1990	24 713	6 674	31 387	– 29 136	– 4 015	– 33 151		– 1 764
1990-1991	26 500	6 972	33 472	– 32 010	– 4 437	– 36 447		– 2 975
1991-1992	28 197	6 747	34 944	– 34 579	– 4 666	– 39 245		– 4 301
1992-1993	28 105	7 764	35 869	– 36 143	– 4 756	– 40 899		– 5 030
1993-1994	28 767	7 762	36 529	– 36 136	– 5 316	– 41 452		– 4 923
1994-1995	29 411	7 494	36 905	– 36 844	– 5 882	– 42 726		– 5 821
1995-1996	30 604	8 126	38 730	– 36 643	– 6 034	– 42 677		– 3 947
1996-1997	31 134	6 704	37 838	– 35 195	– 5 855	– 41 050		– 3 212
After reform of government accounting								
1997-1998	35 754	5 974	41 728	– 36 543	– 7 342	– 43 885		– 2 157
1998-1999	38 517	8 071	46 588	– 39 275	– 7 187	– 46 462		126
1999-2000	40 944	6 334	47 278	– 39 899	– 7 372	– 47 271		7
2000-2001	42 772	8 145	50 917	– 41 934	– 7 606	– 49 540	– 950	427
2001-2002	40 872	9 305	50 177	– 43 844	– 7 261	– 51 105	950	22
2002-2003	43 018[3]	9 307	52 325[3]	– 45 934	– 7 085	– 53 019		– 694
2003-2004[P]	44 654[3]	9 875	54 529[3]	– 47 629	– 7 264	– 54 893		– 364

P: Preliminary results.

1 A negative entry indicates a financial requirement and a positive entry, a source of financing.

2 In addition to the Consolidated Revenue Fund, these data include the revenue and expenditure of the consolidated organizations, which appear in Table 4.1.2.

3 Own-source revenue includes the exceptional losses of the Société générale de financement du Québec of $339 million in 2002-2003 and $364 million in 2003-2004.

Non-budgetary transactions					
Investments, loans and advances	Capital expenditures	Retirement plans	Other accounts	Excess amount (shortfall)	Net financial surplus (requirements)
– 73		2	26	– 45	– 190
– 63		1	113	51	– 304
– 53		– 1	18	– 36	– 383
– 122		25	459	362	– 297
– 146		104	319	277	– 165
– 186		109	622	545	– 406
– 183		187	– 161	– 157	– 1 333
– 229		265	– 488	– 452	– 1 156
– 189		316	119	246	– 1 252
– 188		683	551	1 046	– 1 354
– 56		822	416	1 182	– 2 299
– 586		1 007	71	492	– 2 129
– 761		1 051	– 40	250	– 2 213
– 672		1 057	– 436	– 51	– 2 215
– 167		1 183	887	1 903	– 1 970
40		1 269	493	1 802	– 1 671
– 380		1 355	260	1 235	– 1 737
– 680		2 203	– 493	1 030	– 1 366
– 670		1 634	– 265	699	– 1 005
– 516		1 164	300	948	– 816
– 458		1 874	77	1 493	– 1 482
– 411		1 916	141	1 646	– 2 655
– 490		1 525	82	1 117	– 3 913
– 623		1 668	52	1 097	– 3 826
– 1 142		1 509	578	945	– 4 876
– 287		1 701	– 415	999	– 2 948
– 792		1 928	– 60	1 076	– 2 136
– 1 315	– 209	1 888	109	473	– 1 684
– 1 402	– 217	1 020	996	397	523
– 2 006	– 359	1 740	1 328	703	710
– 1 632	– 473	1 793	– 631	– 943	– 516
– 1 142	– 995	2 089	– 589	– 637	– 615
– 1 649	– 1 482	2 007	240	– 884	– 1 578
– 1 077	– 978	2 221	– 1 235	– 1 069	– 1 433

TABLE 4.1.4

CONSOLIDATED DEBT AT THE END OF THE FISCAL YEAR
(millions of dollars)

	Total debt									
			Retirement plans							
	Direct debt[1,2]		Gross liability of retirement plans		Retirement plans sinking fund		Net liability of retirement plans[3]		Total	
	In $M	As a % of GDP	In $M	As a % of GDP	In $M	As a % of GDP	In $M	As a % of GDP	In $M	As a % of GDP
Before reform of government accounting										
1970-1971	2 478	10.9							2 478	10.9
1971-1972	2 920	11.9							2 920	11.9
1972-1973	3 309	12.0							3 309	12.0
1973-1974	3 679	11.8							3 679	11.8
1974-1975	4 030	11.0					67	0.2	4 097	11.1
1975-1976	4 955	12.0					179	0.4	5 134	12.4
1976-1977	6 035	12.5					354	0.7	6 389	13.2
1977-1978	7 111	13.4					620	1.2	7 731	14.6
1978-1979	8 325	14.1					915	1.6	9 240	15.7
1979-1980	9 472	14.4					1 598	2.5	11 070	16.9
1980-1981	12 247	16.8					2 420	3.3	14 667	20.1
1981-1982	14 184	17.6					3 428	4.3	17 612	21.9
1982-1983	16 485	19.3					4 489	5.3	20 974	24.6
1983-1984	18 880	20.6					5 545	6.0	24 425	26.6
1984-1985	21 216	21.2					6 729	6.7	27 945	27.9
1985-1986	23 633	22.0					7 998	7.5	31 631	29.5
1986-1987	25 606	21.9					9 353	7.9	34 959	29.8
1987-1988	26 819	20.9					10 883	8.5	37 702	29.4
1988-1989	27 091	19.2					12 597	9.0	39 688	28.2
1989-1990	27 699	18.7					14 320	9.6	42 019	28.3
1990-1991	29 637	19.3					16 227	10.6	45 864	29.9
1991-1992	33 106	21.3					18 143	11.7	51 249	33.0
1992-1993	39 231	24.8					19 668	12.4	58 899	37.2
1993-1994	45 160	27.8	21 337	13.2	854	0.5	20 483	12.7	65 643	40.5
1994-1995	52 468	30.8	22 846	13.4	849	0.5	21 997	12.9	74 465	43.7
1995-1996	52 886	29.8	24 547	13.8	923	0.5	23 624	13.3	76 510	43.1
1996-1997	52 625	29.2	26 475	14.7	1 014	0.6	25 461	14.1	78 086	43.3
After reform of government accounting										
1997-1998	57 947	30.7	41 617	22.1	1 179	0.6	40 438	21.5	98 385	52.2
1998-1999	60 685[4]	30.9	42 637	21.7	2 209	1.1	40 428	20.6	101 113[4]	51.5
1999-2000	62 783[4]	29.7	44 377	21.1	5 040	2.4	39 337	18.7	102 120[4]	48.4
2000-2001	65 737[4]	29.2	46 170	20.5	7 059	3.1	39 111	17.4	104 848[4]	46.6
2001-2002	69 115[4]	29.7	48 259	20.7	10 199	4.4	38 060	16.4	107 175[4]	46.1
2002-2003	72 961[4]	29.7	50 266	20.5	11 840	4.8	38 426	15.6	111 387[4]	45.4
2003-2004[P]	76 515[4]	29.6	52 487	20.3	14 204	5.5	38 283	14.8	114 798[4]	44.4

P: Preliminary results.

1 Including Treasury bills, temporary borrowings and long-term debt. Since 1976-1977, the debt in foreign currency has been expressed in the Canadian equivalent based on the exchange rates effective on March 31 of the fiscal year under consideration.

2 Excluding deferred foreign exchange gains or losses.

3 Balance of the liability of the retirement plans less the amount accumulated in the retirement plans sinking fund.

4 Excluding pre-financing totalling $2 831 million in 1998-1999, $506 million in 1999-2000, $1 475 million in 2000-2001, $1 154 million in 2001-2002, $3 967 million in 2002-2003 and $1 644 million in 2003-2004. Including pre-financing, the total debt reached $103 944 million in 1998-1999, $102 626 million in 1999-2000, $106 323 million in 2000-2001, $108 329 million in 2001-2002, $115 354 million in 2002-2003 and $116 442 million in 2003-2004.

Financial assets net of other liabilities[5]		Net debt		Capital expenditures		Debt representing accumulated deficits[6]	
In millions of dollars	As a % of GDP	In millions of dollars	As a % of GDP	In millions of dollars	As a % of GDP	In millions of dollars	As a % of GDP
188	0.8	2 290	10.1			2 290	10.1
275	1.1	2 645	10.8			2 645	10.8
317	1.2	2 992	10.9			2 992	10.9
28	0.1	3 651	11.7			3 651	11.7
4	0.0	4 093	11.1			4 093	11.1
90	0.2	5 044	12.2			5 044	12.2
36	0.1	6 353	13.2			6 353	13.2
673	1.3	7 058	13.4			7 058	13.4
780	1.3	8 460	14.4			8 460	14.4
234	0.4	10 836	16.5			10 836	16.5
341	0.5	14 326	19.6			14 326	19.6
5 043	6.3	12 569	15.6			12 569	15.6
5 936	7.0	15 038	17.6			15 038	17.6
7 127	7.8	17 298	18.8			17 298	18.8
6 490	6.5	21 455	21.4			21 455	21.4
5 896	5.5	25 735	24.0			25 735	24.0
6 243	5.3	28 716	24.5			28 716	24.5
6 587	5.1	31 115	24.2			31 115	24.2
6 869	4.9	32 819	23.3			32 819	23.3
7 436	5.0	34 583	23.3			34 583	23.3
8 306	5.4	37 558	24.5			37 558	24.5
9 364	6.0	41 885	27.0			41 885	27.0
11 985	7.6	46 914	29.6			46 914	29.6
13 806	8.5	51 837	32.0			51 837	32.0
16 788	9.8	57 677	33.8			57 677	33.8
14 886	8.4	61 624	34.8			61 624	34.8
13 253	7.3	64 833	35.9			64 833	35.9
9 788	5.2	88 597	47.0	6 016	3.2	82 581	43.8
15 134[7]	7.7	88 810	45.3	6 233	3.2	82 577	42.1
13 464[7]	6.4	89 162	42.3	6 693	3.2	82 469	39.1
17 165[7,8]	7.6	89 158	39.6	7 166	3.2	81 992[8]	36.4
15 557[7]	6.7	92 772	40.2	8 234	3.6	84 538	36.6
19 897[7]	8.1	95 457	38.9	9 716	4.0	85 741[9]	34.9
19 643[7]	7.6	96 799	37.4	10 694	4.1	86 105	33.3

5 Including deferred foreign exchange gains or losses.
6 Including various accounting restatements that have not undergone a surplus (deficit) adjustment for previous years.
7 Taking into account pre-financing totalling $2 831 million in 1998-1999, $506 million in 1999-2000, $1 475 million in 2000-2001, $1 154 million in 2001-2002, $3 967 million in 2002-2003 and $1 644 million in 2003-2004.
8 Including $950 million placed in reserve.
9 Including $215 million stemming from the correction of the CCRA's error, posted to the debt representing accumulated deficits.

TABLE 4.1.5

CONSOLIDATED DEBT SERVICE
(millions of dollars)

	Consolidated direct debt service				Interest ascribed to the retirement plans[1]		Total debt service	
	Consolidated Revenue Fund	Consolidated organizations	Total					
	In millions of dollars		In millions of dollars	As a % of budgetary revenue	In millions of dollars	As a % of budgetary revenue	In millions of dollars	As a % of budgetary revenue
Before reform of government accounting								
1970-1971	197	—	197	5.2			197	5.1
1971-1972	210	—	210	4.8			210	4.7
1972-1973	242	—	242	4.9			242	4.8
1973-1974	288	—	288	5.1			288	5.0
1974-1975	296	—	296	4.1			296	4.1
1975-1976	368	—	368	4.5			368	4.4
1976-1977	456	—	456	4.8			456	4.7
1977-1978	606	—	606	5.5			606	5.5
1978-1979	763	—	763	6.5	54	0.4	817	6.9
1979-1980	882	—	882	6.7	88	0.6	970	7.3
1980-1981	1 217	—	1 217	8.4	165	1.1	1 382	9.4
1981-1982	1 686	—	1 686	9.5	264	1.5	1 950	10.9
1982-1983	1 921	—	1 921	9.7	379	1.9	2 300	11.5
1983-1984	2 031	—	2 031	9.3	480	2.2	2 511	11.4
1984-1985	2 414	—	2 414	10.8	598	2.6	3 012	13.4
1985-1986	2 648	—	2 648	11.0	706	2.9	3 354	13.8
1986-1987	2 754	—	2 754	10.8	802	3.1	3 556	13.8
1987-1988	2 751	—	2 751	9.7	924	3.2	3 675	12.9
1988-1989	2 665	—	2 665	8.9	1 137	3.8	3 802	12.6
1989-1990	2 829	—	2 829	9.0	1 186	3.7	4 015	12.7
1990-1991	3 026	—	3 026	9.0	1 411	4.2	4 437	13.2
1991-1992	3 222	—	3 222	9.2	1 444	4.1	4 666	13.3
1992-1993	3 475	—	3 475	9.7	1 281	3.5	4 756	13.2
1993-1994	3 750	—	3 750	10.3	1 566	4.3	5 316	14.5
1994-1995	4 333	—	4 333	11.7	1 549	4.2	5 882	15.9
1995-1996	4 287	—	4 287	11.1	1 747	4.5	6 034	15.5
1996-1997	3 906	—	3 906	10.3	1 949	5.1	5 855	15.4
After reform of government accounting								
1997-1998	3 800	577	4 377	10.5	2 965	7.1	7 342	17.6
1998-1999	4 159	614	4 773	10.2	2 414	5.2	7 187	15.4
1999-2000	4 119	621	4 740	10.0	2 632	5.6	7 372	15.6
2000-2001	4 378	634	5 012	9.8	2 594	5.1	7 606	14.9
2001-2002	3 970	574	4 544	9.1	2 717	5.4	7 261	14.5
2002-2003	3 888	549	4 437	8.5	2 648	5.0	7 085	13.5
2003-2004[P]	3 926	596	4 522	8.3	2 742	5.0	7 264	13.3

P: Preliminary results.
1 Amount of interest ascribed to the liability of the retirement plans less the revenue from the retirement plans sinking fund.

Section 5

Debt Control Measures

Factors that increase the debt **3**

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Investments in fixed assets 4
Income earned by government corporations but not paid out as dividends 5

Measures to better control the debt **6**

Review of the mandate of government corporations that invest in venture capital 6
Policy respecting the public sector's fixed assets 7

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This section describes the measures the government intends to adopt to better control the growth of the debt.

Factors that increase the debt

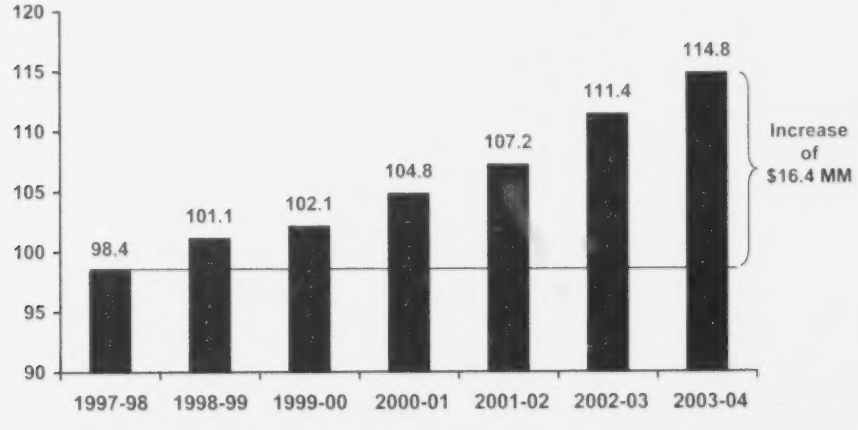
In 1997-1998, the Québec government implemented a major accounting reform, which complies with the accounting standards recommended for the public sector by the Canadian Institute of Chartered Accountants (CICA). It may therefore seem surprising to note that, despite the fact that the government has achieved a balanced budget, its total debt increased by $16.4 billion from 1998-1999 to 2003-2004. It is thus important to clearly understand the factors that have contributed to this increase.

The increase in the total debt is due mainly to three factors:

- government investments in certain government corporations;
- investments in fixed assets;
- income earned by government corporations but not paid out as dividends.

GRAPH 5.1

CHANGE IN THE TOTAL DEBT OF THE GOUVERNEMENT DU QUÉBEC
(billions of dollars)



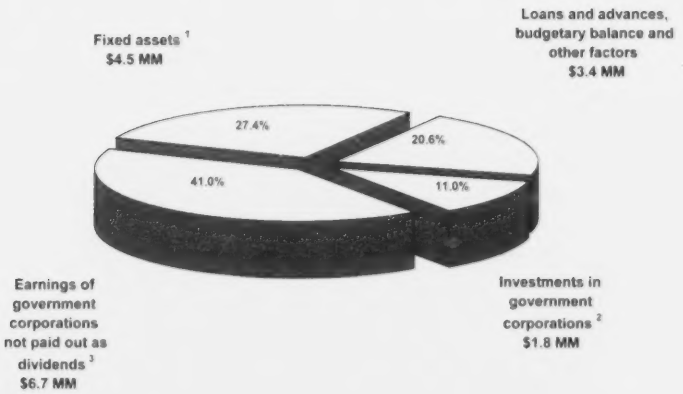
Source: Ministère des Finances du Québec.

Investments in government corporations

Between 1998-1999 and 2003-2004, the amounts invested by the government in its corporations amounted to $1.8 billion. Of this amount, $1.3 billion was invested in the Société générale de financement (SGF) and $400 million in Innovatech corporations. Since the government did not have the funds required at its disposal, it was obliged to borrow them in order to make these investments.

GRAPH 5.2

FACTORS RESULTING IN AN INCREASE OF $16.4 BILLION IN THE GOVERNMENT'S TOTAL DEBT FROM 1998-1999 TO 2003-2004



Source: Ministère des Finances du Québec.

1 Including $3.7 billion for the road system and $0.8 billion for other fixed assets.

2 Including $1.3 billion in the Société générale de financement (SGF), $0.4 billion in Innovatech corporations and $100 million in other corporations.

3 Including over $4.3 billion for which Hydro-Québec is responsible and $2.5 billion for which the CSST is responsible.

Investments in fixed assets

The cost of the fixed assets purchased by the government is capitalized and charged to expenditure based on the useful life of these assets, in accordance with CICA public-sector accounting standards. This means that even in the context of a balanced budget, the government is obliged to borrow sufficient funds to cover the full cost of the fixed assets thus purchased.

From 1998-1999 to 2003-2004, investments in fixed assets boosted the government's total debt by $4.5 billion, $3.7 billion of which was invested in the road system.

Income earned by government corporations but not paid out as dividends

The government includes the total earnings of its government corporations in its income. However, in the case of certain corporations, such as Hydro-Québec, the government does not receive all of their earnings in the form of dividends. In such cases, the government allows these corporations to retain a portion of their earnings so that they can finance their investments, which is the equivalent of making an investment corresponding to the amount of the earnings these corporations do not pay as dividends. This entails an increase in the debt, since the government is obliged to borrow a sum equal to the investment.

Between 1998-1999 and 2003-2004, the government borrowed $6.7 billion for this purpose, thereby increasing its debt accordingly. Of this amount, Hydro-Québec, whose dividends paid to the government represented roughly 50% of its earnings, is responsible for over $4.3 billion, while the CSST, which paid no dividends to the government and was included in its reporting entity up until 2003-2004, accounts for $2.5 billion.

Measures to better control the debt

The government is implementing two measures to better control the growth of its debt, namely:

— the review of its policy respecting investments in its government corporations, especially those that invest in venture capital;

— the drafting of a policy respecting the public sector's fixed assets.

Review of the mandate of government corporations that invest in venture capital

In 2003-2004, the government reduced its investments in the Société générale de financement (SGF) and Innovatech corporations, both of which are government corporations that invest in venture capital. These investments, which were initially forecast at $300 million for 2003-2004, were lowered to $12 million, for a total reduction of $288 million.

In accordance with its debt control measures, the government will review the mandate of government corporations whose mission is to support economic development essentially by stimulating investment in the private sector. In addition, the government intends to exercise tighter control over the amounts it invests in these corporations, in particular by requiring that they:

— set specific goals in terms of planning and monitoring results;

— establish clear objectives with regard to the earnings anticipated in the medium term;

— self-fund their investment projects.

This new approach will entail a significant reduction in investments, thereby curbing the growth of the government's total debt.

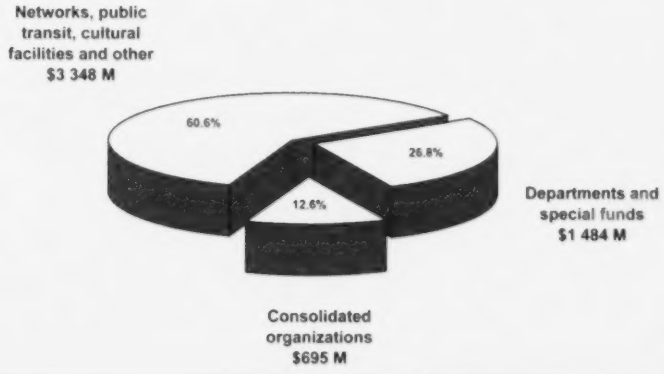
Policy respecting the public sector's fixed assets

Each year, the government authorizes the investments in fixed assets made by its departments, special funds and consolidated organizations. These investments raise the government's debt accordingly, since the amounts required are borrowed in full. These investments will amount to $2.2 billion in 2004-2005.

The government also authorizes a sizeable portion of the investments in fixed assets made by other public-sector institutions, including those made by the education and health and social services networks and funds invested in cultural facilities and public transit. Although these investments impact on the public-sector debt rather than on that of the government, the latter's authorization is required because it assumes, in whole or in part, the ensuing debt service costs. In 2004-2005, these investments will total over $3.3 billion.

GRAPH 5.3

PUBLIC-SECTOR INVESTMENTS IN FIXED ASSETS OF $5.5 BILLION PROJECTED FOR 2004-2005[1]


Networks, public transit, cultural facilities and other $3 348 M
60.6%
26.8%
12.6%
Departments and special funds $1 484 M
Consolidated organizations $695 M

Source: Secrétariat du Conseil du trésor, *Additional Information on the 2004-2005 Expenditure Budget*.

1 Including the share of the government and its partners.

Over the past year, the government has taken concrete action to review its priorities in terms of investments in fixed assets, and re-examined several major development projects.

For example, in the fall of 2003, the government terminated GIRES, a project that would have required an investment of $400 million.

During the coming year, the government will adopt a new policy on investing in fixed assets. The main goals of this policy are to:

— review and fine-tune the planning, authorization, monitoring and accountability arrangements to be implemented by its departments and organizations;

— determine the level of investment that will enable the government to preserve and maintain its public infrastructure while respecting its ability to pay;

— examine new approaches, such as the forging of business partnerships between the public and private sectors, to help cushion the impact of investments in fixed assets on both the government's debt and that of the public sector.

Lastly, the government will exercise greater control over the borrowings and financial transactions of certain government corporations and organizations because it assumes, in whole or in part, the debt service. In particular, it will provide clarifications on:

— the terms and conditions governing the authorization of borrowings;

— the conditions under which derivatives and cash products may be used;

— the financial instruments most likely to minimize the risks associated with refinancing borrowings.

Conclusion

In its Budget of June 12, 2003, the government expressed its concern about the increase in its total debt.

Today, the government has adopted measures that will help it better control the growth of its debt. These measures include:

— a review of the mandate of government corporations, especially those that invest in venture capital;

— the drafting and implementation of a policy respecting public-sector investments in fixed assets.

The measures proposed to better control the debt and the ensuing interest expenses are the first step toward restoring the leeway needed to adequately fund public services and reduce the tax burden.

Section 5 Appendix 5.1

Main debt concepts used

Main debt concepts used

Government debt

Three debt concepts are used for the Québec government:

— the government's total debt;
— the net debt;
— the debt representing accumulated deficits.

Total debt is the amount of the direct debt, which corresponds to the borrowings contracted on the financial markets by the government and its consolidated organizations, plus the value of the government's commitment in respect of its employees' pension plans.

Net debt is obtained by subtracting financial assets from the total debt. Financial assets include investments in government corporations, earnings not paid out as dividends by government corporations, loans and advances granted to third parties and other short-term assets and liabilities.

The debt representing accumulated deficits is obtained by subtracting the undepreciated balance of fixed assets from the net debt.

Public-sector debt

The public-sector debt includes, in addition to the government's total debt, the debts of the education and health and social services networks, Hydro-Québec, municipalities and other government enterprises.

TABLE 5.1.1

DEBT AS AT MARCH 31, 2004[P]
(millions of dollars)

Public-sector debt	**181 764**
Less:	
Education and health and social services networks	10 885
Hydro-Québec	34 776
Other government enterprises	3 535
Municipalities and municipal bodies	17 770
Total government debt[1]	**114 798**
Less: financial assets[1]	17 999
Net debt	**96 799**
Less: undepreciated balance of fixed assets	10 694
Debt representing accumulated deficits	**86 105**

P: Preliminary results.
1 Excluding advance borrowings of $1 644 million, which will be used to cover part of the 2004-2005 borrowings program.

Section 5 Appendix 5.2

Principal factors responsible for the growth of the debt

TABLE 5.2.1

PRINCIPAL FACTORS RESPONSIBLE FOR THE GROWTH OF THE GOVERNMENT'S TOTAL DEBT
(millions of dollars)

	Investments, loans and advances							Fixed assets[1]						
		Earnings not paid out as dividends												
	Investments in government corporations	Hydro-Québec	CSST	Other enterprises	Total	Other loans and advances	Total	Road system	Other	Total	Consolidated budgetary balance	Other factors	Total	Total debt
1997-1998														98 385
1998-1999	184	475	631	176	1 282	– 64	1 402	430	– 213	217	– 126	1 235	2 728	101 113
1999-2000	207	637	787	358	1 782	17	2 006	438	– 79	359	– 7	– 1 351	1 007	102 120
2000-2001	425	621	443	93	1 157	50	1 632	442	31	473	– 427	1 050	2 728	104 848
2001-2002	648	487	– 33	– 83	371	123	1 142	700	295	995	– 22	212	2 327	107 175
2002-2003	340	1 077	680	– 474	1 283	178	1 801	1 150	321	1 471	694[2]	246	4 212	111 387
Subtotal	**1 804**	**3 297**	**2 508**	**70**	**5 875**	**304**	**7 983**	**3 160**	**355**	**3 515**	**112**	**1 392**	**13 002**	
2003-2004[P]	12	1 060		– 206	854	211	1 077	502	476	978	364[3]	992	3 411	114 798
Total	**1 816**	**4 357**	**2 508**	**– 136**	**6 729**	**515**	**9 060**	**3 662**	**831**	**4 493**	**476**	**2 384**	**16 413**	

P: Preliminary figures.

1 The fixed assets are reduced by the yearly depreciation expenditure.

2 The budgetary deficit includes an exceptional loss of $339 million by the SGF.

3 Deficit arising from an exceptional loss of $364 million by the SGF.

Section 5 Appendix 5.3

Principal measures used in other Canadian jurisdictions to balance the budget and control debt

Principal measures used in other Canadian jurisdictions to balance the budget and control debt

British Columbia

2002

— Adoption of the *Balanced Budget and Ministerial Accountability Act*.

- Ministers who do not achieve budget objectives are subject to a salary holdback of 20%.

Alberta

1993

— Adoption of the *Deficit Elimination Act*.

1995

— Adoption of the *Balanced Budget and Debt Retirement Act*, which replaced the *Deficit Elimination Act*.

1999

— Adoption of the *Fiscal Responsibility Act*, which replaced the *Balanced Budget and Debt Retirement Act*.

2003

— Creation of a contingency reserve to cover extraordinary expenditures (for example, in the case of natural disasters). Once the reserve's projected maximum, i.e. $2.5 billion, is attained, the surpluses will be used to repay the debt or paid into a capital fund.

Saskatchewan

1995

— Adoption of the *Balanced Budget Act*. This act requires, among other things, that budget surpluses be applied to debt reduction.

2000

— Adoption of the *Fiscal Stabilization Fund Act* to promote better fiscal planning, given that the surpluses can ultimately be used if a deficit is posted.

Manitoba

1995

— Adoption of the *Balanced Budget, Debt Repayment and Taxpayer Accountability Act*. This act provides for, among other things:

- the holding of a referendum to authorize major tax rate increases or a debt reduction plan;
- a reduction in ministers' salaries if a negative budget balance is not offset by a positive balance the following year.

New Brunswick

1995

— Adoption of the *Balanced Budget Act*.

2001

— Adoption of the *Fiscal Stabilization Fund Act* for the purpose of balancing the budget from year to year.

Nova Scotia

2000

— Adoption of the *Financial Measures Act.*

- Provides for, among other things, the achievement of a balanced budget.

2003

— Announcement of the province's intention to adopt a debt reduction plan that includes three components:

- the creation of a contingency reserve to be used for paying down the net debt;
- use of the net proceeds of disposition and the selling off of the holdings of Crown corporations to reduce pension liability;
- legislation obliging the government to use extraordinary revenues, i.e. those not associated with normal activities or one-time federal transfers, to reduce pension liability.

Ontario

1999

— Adoption of the *Balanced Budget and Taxpayer Protection Act.*

- Stipulates, among other things, that voter approval must be sought through a referendum before the government can raise tax rates or introduce new taxes.

Canada

— No legislative measure has been adopted with regard to budget balance or debt reduction.

— However, the federal government's fiscal policy provides for:

- the creation of a contingency reserve;
- the use of prudent economic assumptions that foster the amassing of budget surpluses.

— At the end of the year, the budget surpluses go toward paying down the net debt.

— In the 2004-2005 Budget, the federal government announced its objective of reducing the net debt-to-GDP ratio to 25% over the next 10 years.

Section 6

Report on the Application of the *Balanced Budget Act*

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Compliance with the requirements of the Act 3

Summary

The *Act respecting the elimination of the deficit and a balanced budget* was adopted unanimously by the National Assembly of Québec on December 19, 1996.

The Act was amended on in the fall of 2001, when the *Act to establish a budgetary surplus reserve fund* was adopted, in order to adapt it to the new budgetary context. Since that time, the Act has been known as the *Balanced Budget Act*.

Under section 15[1] of the Act, the Minister of Finance is required to report in the Budget Speech on the application of the Act.

Compliance with the requirements of the Act

The government achieved surpluses in certain years in relation to the objectives set by the Act:

— under section 9[2] of the Act, deficits may be incurred up to the amount of surpluses accumulated;

— as indicated in Table 6.1, accumulated surpluses were reduced to $1 177 million at the end of the 2002-2003 fiscal year, given the consolidated deficit of $694 million posted for that year.

TABLE 6.1

SURPLUSES ACCUMULATED FROM 1996-1997 TO 2002-2003 UNDER THE *BALANCED BUDGET ACT*
(millions of dollars)

	1996-1997	1997-1998	1998-1999	1999-2000	2000-2001	2001-2002	2002-2003
Deficit provided for by the Act	– 3 275	– 2 200	– 1 200	—	—	—	—
Budgetary balance[1]	– 3 217	– 2 192	126	30	427	22	– 694
Surpluses (overruns)	**58**	**8**	**1 326**	**30**	**427**	**22**	**– 694**
Accumulated surpluses, end of year	**58**	**66**	**1 392**	**1 422**	**1 849**	**1 871**	**1 177**

1 Consolidated surplus (deficit) disclosed in the public accounts.

1 The first paragraph of section 15 stipulates that "the Minister shall report to the National Assembly in the Budget Speech on the objectives pursued by this Act, on the achievement of those objectives and on the variance recorded, if any."

2 Section 9 stipulates that "if the Government achieves a surplus in a fiscal year, it may incur overruns in subsequent fiscal years up to the amount of that surplus."

In 2003-2004, the consolidated budgetary deficit of $364 million, after the exceptional losses of the Société générale de financement du Québec (SGF), will reduce accumulated surpluses to $813 million.

TABLE 6.2

ANTICIPATED ACCUMULATED SURPLUSES UNDER THE *BALANCED BUDGET ACT*
(millions of dollars)

	2003-2004[1]
Accumulated surpluses, beginning of year	1 177
Surpluses (overruns)	– 364
Accumulated surpluses, end of year	**813**

1 Preliminary results.

Section 7

Review of tax expenditures and corporate taxation

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Review of tax expenditures

In the *2003-2004 Budget Speech*, the government significantly reduced the level of tax expenditures:

- elimination of 19 fiscal measures including 12 associated with designated sites;
- reduction in the level of assistance of 22 fiscal measures, i.e. a decline in the rates of tax credits of 12.5% or 25%, as the case may be, and a reduction in tax holidays of 25%;
- implementation of moratoriums on certain fiscal measures intended for the capitalization of businesses and for investment.

These tightening measures enabled the government to save $107 million in 2003-2004 and $626 million in all over a full year.

Accordingly, the cost of tax assistance for businesses[1] fell from $2.1 billion to $1.6 billion, a decline of 27%.

Tax expenditures[2]

"Tax expenditures" are revenues the government agrees to forego in order to reduce the tax load on taxpayers – businesses or individuals – by exempting them from certain provisions of the basic tax system that would normally apply.

Tax expenditures can take many forms: exemptions, deductions in calculating income, and tax credits.

In the government's financial statements, tax expenditures are recorded in budgetary revenue and not as expenditures, since these tax expenditures reduce the tax revenues collected from businesses and individuals.

1 To estimate the tax expenditures introduced in support of businesses as accurately as possible, only the tax expenditures defined for this objective have been grouped under the term "tax assistance". The concept of tax assistance thus excludes tax expenditures such as those allowing the carry-over of losses or the deduction of depreciation expenditures in calculating income. Some tax expenditures relating to the personal income tax system, designed to facilitate the capitalization of businesses, have also been added.

2 Tax expenditures are quantified and shown in detail in *Tax Expenditures*, 2003 Edition, ministère des Finances du Québec, 184 pages.

The *2003-2004 Budget Speech* also indicated that the government intended to continue to analyze all existing tax expenditures to ensure that they make an optimal contribution to the development of Québec's economy.

This analysis has been fuelled by the comments received during the prebudget consultations.

What has emerged from this exercise is that the government must continue to support the efforts of businesses because they are essential to promoting an increase in overall wealth.

Accordingly, in the *2004-2005 Budget Speech*,[3] the government is:

— reaffirming its support for economic activities considered as priorities, such as research and development (R&D);

— improving or refocusing some fiscal measures to achieve specific economic development objectives, such as diversification of activities in the resource regions.

Moreover, the government cannot ignore existing budgetary constraints and the fact that some tax expenditures no longer correspond to their initial objectives. Accordingly, the government is:

— eliminating or tightening certain tax expenditures that have had mixed results.

3 The measures mentioned in this section are discussed in detail in the document *Additional Information on the 2004-2005 Fiscal Measures* that, in this regard, is the reference source.

❑ *Total savings on tax expenditures of $813 million*

The tightening of tax expenditures introduced in this Budget Speech will total $187 million.

Adding these to the tightening measures announced in the *2003-2004 Budget Speech*, reductions in tax expenditures will reach $813 million over a full year.

TABLE 1

ILLUSTRATION OF THE IMPACT OVER A FULL YEAR OF THE ADJUSTMENTS TO TAX ASSISTANCE FOR BUSINESSES INTRODUCED IN THE 2003-2004 AND 2004-2005 BUDGET SPEECHES
(Millions of dollars)

	Tightening measures	Tax assistance
Tax assistance for businesses initially stipulated in 2004-2005		**2 148**
Tightening measures		
▪ Measures in the *2003-2004 Budget Speech*	-626	
▪ Measures in the *2004-2005 Budget Speech*	-187	
Total tightening measures – individuals and businesses	**-813**	
▪ Personal income tax measures[1]	116	
▪ Tax assistance improvement measures	63	
Total tightening measures – tax assistance for businesses	**-634**	
Tax assistance for businesses after tightening measures		**1 514**
Per cent reduction		**-30%**

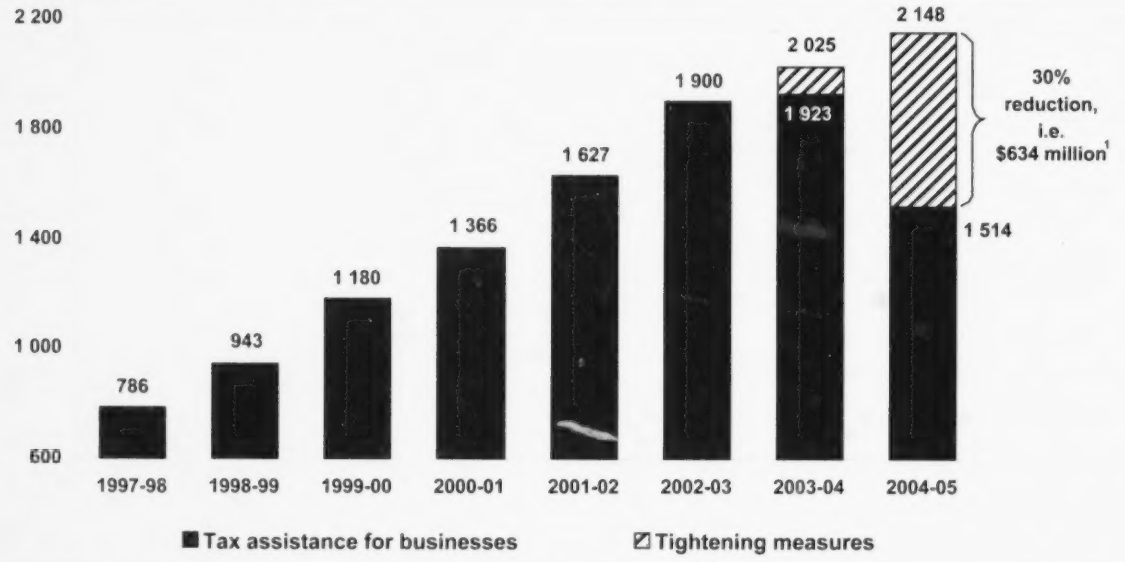
1 Isolates the impact of tightening measures regarding tax assistance for businesses by excluding measures targeting high-income individuals and certain other measures.

❑ *Total reduction of 30% in tax assistance for businesses*

Cuts in tax assistance for businesses will reach $634 million over a full year.[4] This represents a decline of 30% compared to total tax assistance for businesses estimated prior to the June 12, 2003 Budget Speech and relating to fiscal year 2004-2005.

CHART 1

TAX ASSISTANCE TO BUSINESSES
(Millions of dollars)



1 Impact over a full year of the tightening measures of the *2003-2004 Budget Speech* and of measures of the *2004-2005 Budget Speech* shown on the basis of the cost of tax assistance initially stipulated for 2004-2005.

4 This amount is obtained by subtracting from the total tightening measures introduced by this government the improvements put in place and the tightening measures that apply to individuals. See Table 1.

❑ *Strategic measures maintained and bolstered*

The *2004-2005 Budget Speech* confirms the continuation and improvement of fiscal measures that contribute to:

- growth in R&D activities of Québec companies that want to improve their productivity and competitiveness on international markets, for an amount of $459 million;

- the development of the resource regions, suffering from economies with little diversification that make dynamic occupation of the territory difficult, for an amount of $153 million;

- the preservation of Québec's cultural identity, for an amount of $105 million.

Considering the measures in this Budget Speech, the financial support granted by the government to develop strategic activities and sectors will exceed $1.5 billion.

TABLE 2

BREAKDOWN OF TAX ASSISTANCE MEASURES FOR BUSINESSES
(Millions of dollars)

	2004-2005
Tax credits and tax holidays	
▪ Research and development	459
▪ Investment	314
▪ New economy	278
▪ Regions	153
▪ Culture	105
▪ Other	40
Subtotal	1 349
Business capitalization	165
TOTAL	**1 514**

Source: Ministère des Finances du Québec.

1. Enhancing certain fiscal measures

The government is improving certain fiscal measures to better achieve its strategic objectives and correct specific problems.

These improvements will be of benefit particularly to companies located in the regions and will stimulate especially processing, natural resources exploration, manpower training, innovation and cooperative capitalization activities.

1.1 Measures relating to the regions

Tax credits for processing activities in the resource regions

Specific tax credits apply to the resource regions:

— a refundable tax credit for processing activities in the resource regions;

— a refundable tax credit for the Vallée de l'aluminium, located in Saguenay–Lac-Saint-Jean;

— a refundable tax credit for Gaspésie and certain maritime regions of Québec.

Briefly, these tax credits, whose rate is 30%, are granted regarding jobs created by a corporation operating in one of Québec's resource regions, for a period of five years.

Currently, more than 400 companies benefit from these fiscal measures.

❑ ***Three-year extension of eligibility for tax credits***

Eligibility for these tax credits is scheduled to end on December 31, 2004. However, the lumber crisis and the closing of many plants that are key to the activity of certain regions are hampering their development of the resource regions.

To continue to assist the resource regions in their economic diversification efforts, the government is announcing a three-year extension of the eligibility period for these tax credits. Accordingly, projects submitted until December 31, 2007 may be eligible for tax assistance.

This initiative will in particular help Gaspésie in its efforts to develop the promising wind-power sector.

❑ ***Reintroduction of eligibility of specialized equipment manufacturing activities for tax assistance***

In view of the positive impact of these activities on the economic development of the resource regions, the government is announcing the reintroduction of eligibility of specialized equipment manufacturing activities for tax assistance.

In addition, tax assistance targeting equipment makers will henceforth be available in all the resource regions.

— The reintroduction of eligibility of specialized equipment manufacturing activities will be of particular benefit for Saguenay–Lac-Saint-Jean, where many equipment makers are located.

— Moreover, the Saguenay–Lac-Saint-Jean will continue to enjoy exclusivity regarding products made or processed from aluminum that has undergone primary processing.

❑ ***Improvement of the tax credit for Gaspésie and certain maritime regions of Québec***

Improvements will be made to the refundable tax credit for Gaspésie and certain maritime regions of Québec, in particular to further support mariculture and marine biotechnology. These improvements are being made to take into consideration the particularly difficult employment situation in these regions.

— The rate of the tax credit, calculated on wages relating to jobs created, will be raised from 30% to 40%.

— Special measures will be taken to enable the mariculture and marine biotechnology sectors to derive more benefit from this tax credit. The tax credit will henceforth be calculated on all the salaries paid to employees working in these activity sectors. Roughly 25 companies will benefit from these improvements specifically targeting these rapidly emerging activities.

— Gaspésie and certain maritime regions of Québec will continue to enjoy exclusivity regarding marine biotechnology, sea products processing and growing, manufacturing of wind generators and the production of wind-power.

TABLE 3

IMPACT OF THE IMPROVEMENT TO TAX CREDITS APPLICABLE IN THE RESOURCE REGIONS

	Tax assistance parameters		Financial impact over a full year (Millions of $)
	Rate	Base	
• Three-year extension of eligibility for tax credits applicable in the resource regions	30%	Wages tied to jobs created	-5
• Reintroduction of eligibility for equipment makers in all the resource regions	30%	Wages tied to jobs created	-4
• Improvement of measures concerning Gaspésie and certain maritime regions	30% to 40%	Wages tied to jobs created or salaries paid in the case of mariculture and marine biotechnology	-3
TOTAL			**-12**

TABLE 4

TAX CREDITS APPLICABLE IN THE RESOURCE REGIONS

Tax credits	Eligible activities	Eligible territories
Processing activities in the resource regions		
• 30% of wages of new employees for five years	• Manufacturing or processing of finished or semi-finished products (including equipment) from wood, paper and cardboard, metals (except aluminum) and non-metallic minerals • Food processing, reclamation and recycling of waste and residual materials resulting from natural resource exploitation or processing, fresh-water aquaculture, production of non-conventional energy, manufacturing of products from peat	• Bas-Saint-Laurent Saguenay–Lac-Saint-Jean Mauricie Abitibi-Témiscamingue Côte-Nord Nord-du-Québec Gaspésie–Îles-de-la-Madeleine Antoine-Labelle RCM Vallée-de-la-Gatineau RCM Pontiac RCM
Vallée de l'aluminium		
• 30% of wages of new employees for five years	• Manufacturing or processing of finished or semi-finished products from aluminum that has undergone primary processing	• Saguenay–Lac-Saint-Jean
Gaspésie and certain maritime regions		
• 40% of wages of new employees for five years	• Transformation of marine products (fish and seafood)	• Gaspésie–Îles-de-la-Madeleine, Côte-Nord and Matane RCM
	• Manufacturing of wind-power generators and production of wind power	• Gaspésie–Îles-de-la-Madeleine and Matane RCM
• 40% of salaries paid for five years	• Mariculture (growing of sea products)	• Gaspésie–Îles-de-la-Madeleine and Côte-Nord
	• Manufacturing of finished or semi-finished products in the marine biotechnology field	• Gaspésie–Îles-de-la-Madeleine, Côte-Nord and Bas-Saint-Laurent

Cooperative Investment Plan

The Cooperative Investment Plan (CIP) is designed to encourage the growth of cooperatives by granting a tax benefit consisting of a deduction to members and workers who acquire units of an eligible cooperative.

The June 12, 2003 Budget Speech announced a moratorium on the CIP regarding the issue of new units giving rise to the deduction. However, the moratorium does not affect labour cooperatives. Moreover, as a contribution to the effort to tighten tax expenditures, the deduction applicable to the acquisition of CIP units was reduced by 25%.

Since its inception in 1985, the CIP has made a significant contribution to the capitalization of cooperatives. Some 250 producer and labour cooperatives have availed themselves of the program and more than $280 million in equity capital has been raised thanks to this measure. The leverage produced by this capital has contributed to the growth in the assets of these cooperatives, from $550 million in 1985 to over $1.6 billion in 2001.

Moreover, environmental pressure, stricter food safety requirements and market globalization are factors pushing farm cooperatives to increase their investments. These cooperatives account for 80% of the sales of non-financial cooperatives.

Accordingly, the government intends to support cooperatives in their efforts to increase their investments. Concretely, this support will be implemented through the following reform:

— The government is lifting the moratorium on this investment vehicle.

— The rate structure will be simplified with the application of a single deduction rate, raised to 125%.

— To reflect the reality of the farm sector, where over 5 000 producers are now incorporated as capital-stock corporations, the government will make the preferred units of eligible cooperatives acquired by shareholders of farm enterprises incorporated as capital-stock corporations eligible for the CIP.

Moreover, the rules on the issue of units eligible for the CIP have been adjusted to ensure that they contribute to an increase in the capitalization of cooperatives. These adjustments include:

— Raising the minimum holding period for CIP units from two years to five years.

— Excluding from the measure producer cooperatives with a sufficiently high capitalization rate. This capitalization rate will be set at 60%.

In the regions, cooperatives are key players promoting economic growth and diversification. The lifting of the moratorium on the CIP and the adjustments to this program will support regional development.

TABLE 5

IMPACT OF CHANGES TO THE COOPERATIVE INVESTMENT PLAN

	Before 2004-2005 Budget	2004-2005 Budget	Financial impact over a full year (Millions of $)
Lifting of the moratorium on producer cooperatives			-7
Changes made:			-4
• Tax deduction rate			
– Deduction allowed workers	93.75% – 112.50%	125%	
– Deduction allowed members	75% – 93.75%	125%	
• Size criterion	Small or medium-size criterion[1] (gives rise to the highest deductions)	Elimination of the size criterion	
• Criterion regarding maximum capitalization rate for producer cooperatives	None	60%	
• Shareholders of farm cooperatives	Not eligible	Eligible	
TOTAL			**-11**

1 Assets less than $25 million or net equity of no more than $10 million.

Tax credit for on-the-job training periods

The current tax system stipulates a refundable tax credit for on-the-job training periods. This tax credit is 30% for corporations and 15% in other cases and applies to salaries paid to interns, apprentices and supervisors. This incentive is designed to align teaching with the needs of businesses and to support them in the development of human capital.

To encourage employers in the remote resource regions[5] to offer training periods to students and thus further promote the retention and hiring of young people, the ceiling on expenditures eligible for the tax credit is being doubled for training periods completed in these regions.

Accordingly, the maximum amount of the tax credit will rise from $187.50 to $375 per week, per participant.

The financial impact of this improvement amounts to $3 million over a full year.

TABLE 6

TAX CREDIT FOR ON-THE-JOB TRAINING PERIODS
(Amounts per week, per participant)

Parameters	Remote resource regions	Elsewhere in Québec
▪ Ceiling on eligible expenditures	$1 000 to $1 250	$500 to $625
▪ Maximum tax credit	$300 to $375	$150 to $187.50

5 Gaspésie–Îles-de-la-Madeleine, Saguenay–Lac-Saint-Jean, Abitibi-Témiscamingue, Nord-du-Québec, Côte-Nord, Bas-Saint-Laurent, Haut-Saint-Maurice RCM, Mékinac RCM, Antoine-Labelle RCM, Vallée-de-la-Gatineau RCM and Pontiac RCM.

Tax credit for new graduates working in a remote resource region

To enable new university, college vocational and secondary vocational graduates to acquire their first job experience in their field of specialization and do so in a remote resource region, a refundable tax credit for new graduates working in remote resource regions will be implemented as part of the *2004-2005 Budget Speech*.

Briefly, this tax credit will correspond to 40% of the salary paid to a young graduate. The amount of the tax credit may not exceed $8 000 per graduate.

This measure is designed to encourage young people to remain in the remote resource regions.

TABLE 7

TAX CREDIT FOR NEW GRADUATES WORKING IN A REMOTE RESOURCE REGION

	Parameters of tax assistance		Financial impact over a full year (Millions of $)
	Rate	Base	
• Tax credit for new graduates working in a remote resource region	40%	Salary earned during 52 weeks of work (maximum tax credit of $8 000)	-13
TOTAL			**-13**

Measures relating to the resource sector

Over the last ten years, Québec's mining industry has had to deal with especially difficult market conditions, marked in particular by a general softening in prices of metallic substances sold on export markets.

In addition to causing certain mines to close, these conditions have kept exploration spending in Québec well below the level required to maintain mineral development potential.

To secure the long-term prospects of Québec's mining industry, not only must the efforts made to diversify marketable substances be continued, but mineral resource development sites must also be renewed as quickly as possible before they are exhausted.

❑ *Flow-through share system*

To support small exploration companies – junior companies –, the government is making permanent the flow-through share system that was to end on December 31, 2004. In addition, the two rates of additional deductions granted to individuals, for exploration work carried out in Québec, will be raised.

— For instance, the maximum deduction rate Québec investors may claim will rise from 131.25% to 150%.

Similarly, the moratoriums on foregoing the issue expenses of flow-through shares and on the additional capital gains exemption in respect of certain resource properties will be lifted.

❑ *Tax credit for resources*

To maintain parity between the assistance provided through the flow-through share system and the tax credit for resources, the refundable portion of the tax credit for resources, applicable to eligible expenditures incurred by junior companies, will also be raised. However, the overall rate of the tax credit – refundable and non-refundable portions – will remain 45%. Accordingly, the net cost to the company or to the investor of an exploration expenditure of $100 made by a junior company will henceforth be $28 in Québec, both in the flow-through share system and regarding the tax credit.

These changes, together with a much more encouraging market outlook and one of the best mineral potentials in the world should encourage the mining industry to increase its exploration activity over the coming years.

TABLE 8

IMPACT OF IMPROVEMENTS TO MEASURES RELATING TO THE RESOURCE SECTOR

	Parameters of tax assistance		Financial impact over a full year (Millions of $)
	Rate	Base	
Flow-through share system			-8
▪ Basic deduction rate	100%	Subscribed shares	
▪ Rate including first additional deduction	110.42% to 125%	Subscribed shares (for mining exploration work in Québec)	
▪ Rate including second additional deduction	131.25% to 150%	Subscribed shares (for surface mining exploration work in Québec or for oil and gas exploration work incurred in Québec)	
Tax credit for resources (junior companies)			-2
▪ Activities relating to mineral resources			
– In a northern exploration zone	33.75% to 38.75%[1]		
– Elsewhere in Québec	30% to 35%[1]		
▪ Activities relating to oil and gas			
– In a northern exploration zone	33.75% to 38.75%	Eligible exploration expenditures	
– Elsewhere in Québec	30% to 35%		
▪ Activities relating to renewable energy and energy conservation	30% to 35%		
TOTAL			-10

1 Refundable portion of the tax credit only. From now until 2008, a non-refundable portion is added, resulting in an overall rate of 45%.

❑ *Summary of measures for the regions*

In the *2004-2005 Budget Speech*, the government is reiterating its support for the resource regions by improving and adding to the tax assistance applicable to them.

In all, these measures represent an additional $49 million allocated for this purpose.

TABLE 9

SUMMARY OF FISCAL MEASURES FOR THE REGIONS
(Millions of dollars)

	Financial impact over a full year
• Tax credits applicable in the resource regions	-12
• Cooperative Investment Plan	-11
• Tax credit for on-the-job training periods	-3
• Tax credit for new graduates working in a remote resource region	-13
• Flow-through share system	-8
• Tax credit for resources	-2
TOTAL	**-49**

1.2 Measures relating to innovation

Tax credit for technology adaptation services

The refundable tax credit for technology adaptation services encourages competitive intelligence and technology transfer services for the benefit of SMEs.

The rate of the tax credit is 30% and applies to eligible expenditures incurred by an SME with an eligible competitive intelligence centre, an eligible liaison and transfer centre or an eligible college technology transfer centre.

To encourage innovation activities in the regions, the government will raise the rate of the tax credit to 50% and broaden eligibility to large companies. These changes will encourage the development of innovative companies and stimulate demand for the services of these centres.

Furthermore, to concentrate more financial resources in the development of technology transfer activities, competitive intelligence services will no longer be eligible for tax assistance.

Biotechnology development centres

A corporation that carries out an innovative project in a biotechnology development centre (CDB) can benefit from the following fiscal measures:

- a tax credit of 30% of the salary paid to an eligible employee until December 31, 2013 (maximum of $11 250 per employee, per year);
- a tax credit of 30% of the cost of eligible specialized equipment for three years;
- a tax credit of 30% of the cost of using eligible specialized facilities for five years;
- a five-year tax holiday corresponding to 75% of income tax, the tax on capital and employer contributions to the Health Services Fund (HSF).

It appears that the definition of innovative project is restrictive and is hampering eligibility for the CDBs in Sherbrooke, Laval, Lévis and Saint-Hyacinthe. Accordingly, this condition will no longer apply and the associated tax holiday will no longer be granted. However, all companies may henceforth benefit fully from the three tax credits that remain applicable. Therefore, more companies may now benefit from the fiscal measures relating to CDBs.

1.3 Measure relating to culture

Tax credit for Québec film and television production

The refundable tax credit for Québec film and television production is designed to encourage the production of Québec films and television programs.

The tax credit covers labour expenditures. The rate of the tax credit is generally 29.1667%.

In the *2003-2004 Budget Speech*, the government excluded certain types of television programs from eligibility for the tax credit, in particular variety programs and daily magazines, as well as theme magazines.

During the prebudget consultations, industry stakeholders demonstrated that the production of these programs is essential to cultural development and the associated jobs.

Consequently, the government will restore eligibility for the tax credit for film and television production for these variety programs and magazines.

TABLE 10

IMPACT OF THE IMPROVEMENT TO THE TAX CREDIT FOR QUÉBEC FILM AND TELEVISION PRODUCTION

	Parameters of tax assistance		Financial impact over a full year (Millions of $)
	Rate	Base	
• Tax credit for film and television production	29.1667%[1]	Salaries paid regarding variety programs and daily magazines as well as theme magazines	-10
TOTAL			**-10**

1 Since the amount of eligible expenditures is limited to 50% of production costs, the effective rate of the tax credit is 14.58335%.

1.4 Measures relating to manpower

Tax holidays for certain foreign employees

The tax holidays granted to certain foreign employees make it easier to recruit non-residents with special skills. Accordingly, such an individual who comes to Québec to work may claim a tax holiday on personal income tax for a maximum of five years.

The individuals in question include, among others, researchers employed by a company that carries out R&D in Québec, post-doctoral research fellows employed by a univeristy or a public research centre and professors employed by a university.

Since the *2003-2004 Budget Speech*, these various tax holidays consist of a deduction in the calculation of the individual's taxable income generally corresponding to an amount equal to 75% of his income.

After considering the application details of these tax holidays and further to the representations received, these tax holidays will be adjusted, though the financial impact will remain largely unchanged.

Accordingly, the deductions relating to tax holidays will be improved to reach 100% of income during the first two years of application. Thereafter, they will be gradually reduced to 25% annually. This adjustment will reduce the inconvenience associated with the sudden disappearance of the tax holiday at the end of the fifth year and will increase the incentive for these foreign employees to settle in Québec.

TABLE 11

TAX HOLIDAYS FOR CERTAIN FOREIGN EMPLOYEES

	Years					Subsequent years
	1	2	3	4	5	
• Existing measure	75%	75%	75%	75%	75%	0%
• New adjusted measure	100%	100%	75%	50%	25%	0%

2. Tightening certain fiscal measures

The purpose of reviewing fiscal measures was to identify those whose efficiency had not been sufficiently demonstrated, those that failed to achieve their objectives and those whose cost could not be justified.

This review was also extended to fiscal measures affecting high-income individuals.

To mitigate the cost of certain incentives, improve the integrity of the tax system and optimize the yield of these measures, the government will introduce tightening measures affecting:

— the tax benefits relating to international financial centres;

— contributions paid to the Fonds de solidarité FTQ, Fondaction and Capital régional et coopératif Desjardins;

— the deduction for investment expenses of an individual;

— the deduction for securities options.

2.1 Measures relating to the financial sector

International financial centres

To maintain leading international financial expertise in Québec, the government implemented tax benefits relating to international financial centres (IFC). Accordingly, provided international financial transactions are carried out in Montréal, the chief benefits regarding an IFC include:

- a tax holiday for corporations that corresponds to 75% of income tax, tax on capital and employer contributions to the HSF;

- a personal income tax holiday for Canadian employees of an IFC that corresponds to an amount equal to 37.5% of their salary;

- a personal income tax holiday granted to foreign specialists employed by an IFC that corresponds to an amount equal to 75% of all their income, for a period of five years.

In recent years, changes were made concerning eligibility for the tax benefits relating to IFCs that have moved them away from their initial objective and, incidentally, made them significantly more expensive. As part of the *2004-2005 Budget Speech*, the government will substantially refocus these tax benefits on their initial objective.

Accordingly, regarding the tax holiday applicable to corporations, changes will be made to exclude, regarding a non-financial business, transactions carried out on behalf of another non-financial business with which it is not at arm's length.

Furthermore, the following changes will be made concerning the tax holiday for employees:

- The tax deduction for Canadian employees will henceforth be accessible only to employees that carry out international financial transactions. In addition, a ceiling of $50 000 will apply to the amount an individual may deduct from his taxable income.

- The deduction for foreign specialists, which corresponds to an amount of 75% of their income for five years, will be changed so that the deduction decreases over five years.

TABLE 12

IMPACT OF TIGHTENING MEASURES REGARDING TAX BENEFITS RELATING TO INTERNATIONAL FINANCIAL CENTRES

	Parameters of tax assistance		Financial impact over a full year (Millions of $)
	Rate	Base	
Tax holiday for corporations	75%	Restrictions on the eligibility of certain international financial transactions Elimination of the exemption concerning the compensatory tax on financial institutions	13
Tax holidays for individuals			12
▪ Canadian employees	37.5%	Introduction of a $50 000 ceiling for the calculation of the deduction applicable to the salary paid by the IFC	
▪ Foreign specialists	75% for five years to a gradual reduction (100% - 100% - 75% - 50% - 37.5%)	Income from all sources	
TOTAL			**25**

2.2 Measures relating to business capitalization

Tax-assisted funds

The support the government has provided for the start-up and development of labour funds, namely the Fonds de solidarité FTQ and Fondaction, and Capital régional et coopératif Desjardins (CRCD), is designed to build a pool of venture capital for the development of Québec SMEs.

Overall, the supply of venture capital is abundant in Québec, though many Québec SMEs still suffer from a lack of financing. This supply is attributable to a large extent to so-called tax-assisted funds, because of the incentives associated with them, resulting in substantial costs for the government that can exceed $200 million per year. For this reason, issues of shares of labour funds and CRCD were capped in the June 12, 2003 Budget Speech.

❑ *Ceilings raised*

New ceilings, higher than last year's, will be applied for next year. The ceilings on issues of tax-assisted funds will be $700 million for the Fonds de solidarité FTQ, $100 million for Fondaction and $100 million for CRCD.

In spite of these limits, labour funds and CRCD will be able to collect substantial amounts. Moreover, they will have to direct more resources to achieving the government's objective of closing the gaps in financing for Québec SMEs, especially in the regions.

TABLE 13

IMPACT OF TIGHTENING MEASURES APPLIED TO TAX-ASSISTED FUNDS

	Ceiling (Millions of $)	Parameters of tax assistance		Financial impact over a full year[1] (Millions of $)
		Rate	Maximum deduction	
Tax-assisted funds				
• Labour funds				
– Fonds de solidarité FTQ	600 to 700	15%	$750 per year	8
– Fondaction	80 to 100	15%	$750 per year	1
• Capital régional et coopératif Desjardins	75 to 100	50%	$1 250 per year	25
TOTAL				**34**

1 On the basis of issues of shares normally carried out.

2.3 Reduction of tax benefits for high-income individuals

As part of the effort to tighten tax expenditures, the government is reducing two such expenditures that mainly affect high-income individuals, namely the deduction for investment expenses and the deduction for securities options.

Deductibility of investment expenses

The current system allows an individual who incurs expenses to earn investment income to deduct them against his income from all sources.

These deductible expenses can consist, in particular, of investment management or administration expenses, fees paid to an investment adviser and interest paid on loans used to acquire bonds, stock, mutual fund units or a participation in a partnership.

Under the current system, an individual who suffers losses in excess of his investment income can deduct his investment expenses against income from other sources, for instance, his employment or business income.

While allowing a deduction for expenditures incurred to earn investment income is justified, the deductibility of investment expenses against income other than investment income is more difficult to justify.

For that reason, expenditures incurred after the day of the *2004-2005 Budget Speech* will be deductible up to the amount of investment income declared in the same year. The portion of expenditures that cannot be deducted may be carried forward to subsequent taxation years.

This restriction concerns the following types of investment income, in particular:

— taxable dividends of taxable Canadian corporations;

— interest from Canadian sources;

— gross foreign investment income;

— taxable capital gains.

Deduction for securities options

Companies can offer their employees, as remuneration, options to purchase securities or mutual fund units. Employees who receive this type of remuneration must include in their income a benefit equal to the difference between the value of the securities at the time of acquisition and the amount paid to acquire them. However, employees can claim a deduction whose rate was reduced from 50% to 37.5% in the June 12, 2003 Budget Speech.

It is difficult to understand that a benefit of this magnitude is allowed for this type of remuneration compared to the salary of other employees. In addition, in many cases, this deduction is used to grant extraordinary benefits to business executives.

For these reasons, the generosity of the deduction for securities options will be reduced. The rate of this deduction will accordingly be lowered from 37.5% to 25%, returning it to the situation prior to February 28, 2000.

TABLE 14

IMPACT OF TIGHTENING MEASURES APPLIED TO CERTAIN TAX BENEFITS AFFECTING HIGH-INCOME INDIVIDUALS

	Parameters of tax assistance		Financial impact over a full year (Millions of $)
	Rate	Base	
Deductions			
▪ Investment expenses	100%	Administration and management, expenses, fees paid to an adviser, interest paid on loans and other Expenditures can be deducted solely against investment income	28
▪ Securities options	37.5% to 25%	Taxable benefit: difference between the value of the security at the time of acquisition and the amount paid to acquire it	13
TOTAL			**41**

3. Eliminating certain fiscal measures

Québec grants tax benefits to companies in many activity sectors. These tax benefits are generally higher than in other jurisdictions. In many cases, they are unique to Québec.

To further rationalize the tax assistance granted to companies and simplify the administration of the tax system, the government is eliminating certain fiscal measures.

Five-year tax holiday for new corporations

The five-year tax holiday for new corporations is designed to encourage the creation of new businesses by reducing the impact of certain taxes and costs tied to the start-up phase.

New corporations can receive a tax holiday for the first five years of operation that corresponds to 75% of the three major corporate tax bases, namely income tax, tax on capital and employer contributions to the HSF.

During the examination of all tax expenditures, a number of reasons convinced the government to eliminate this tax holiday:

— It affects the integrity of the tax system. Currently, certain restrictions are applied to ensure that only new businesses can benefit from this measure. However, experience has shown that the criteria are very complex to administer and do not enable adequate control. For instance, it is very difficult to ensure that the business is not the continuation of an existing business.

— It impairs the fairness of the tax system. It is estimated that 90% of new businesses reproduce an existing activity with technology that is already available in a sector in which competition is often fierce.

— It is aggregated with other incentives. Many government programs providing support, funding and technical assistance already facilitate business start-ups. In addition, a tax holiday is already in place, and remains, for manufacturing SMEs in the regions.

— It chiefly benefits companies providing services and, by the same token, especially encourages economic activities that would occur in any event. It has been shown that only 10% of the total value of the tax holiday was received by corporations operating in the primary and manufacturing sectors.

— It is not a key factor in the decision to invest or create a business in Québec.

— It is an increasingly expensive tax expenditure. The value of the tax holiday amounted to $75 million for 2004. Without the tightening measures introduced in June 2003, the cost of the tax holiday would have approached $100 million. Since 1998, the cost of this fiscal measure has more than doubled.

Only Nova Scotia and Newfoundland and Labrador allow a tax holiday for new corporations. The other provinces prefer to reduce the tax burden on SMEs.

The government intends to reduce the tax burden on all SMEs. It will support them by raising the exemption from the tax on capital, as announced in this Budget Speech.

For these reasons, it has been decided to eliminate the tax holiday for new corporations.

Tax credit for railway businesses

In 1998, the Québec government introduced a refundable tax credit for railway businesses to improve their competitive position. The tax credit is equal to 56.25% of the amount of property taxes payable by a railway operator.

The tax assistance for railways was implemented following the privatization and deregulation of the industry. Large railway companies abandoned their less busy sections to reduce operating costs and become more profitable.

In view of the fact that large railway companies are now competitive and that railways of local interest have thrived and should become self-sufficient, the refundable tax credit for railway businesses will be eliminated as of this Budget Speech.

Moreover, Québec railway businesses continue to enjoy a fuel tax rate and consumption tax system that are among the most advantageous in Canada.

TABLE 15

IMPACT OF THE ELIMINATION OF CERTAIN FISCAL MEASURES

	Parameters of tax assistance		Financial impact over a full year (Millions of $)
	Rate	Base	
▪ Tax holiday for new corporations	75% of the first $200 000 of business income 75% of the tax on capital for the first $3 million of paid-up capital 75% of employer contributions to the HSF for the first $700 000 paid in wages	Income tax, tax on capital and employer contributions to the HSF	75
▪ Tax credit for railway businesses	56.25%	Property taxes relating to railroad rights-of-way	12
TOTAL			**87**

4. Maintaining certain moratoriums

In the *2003-2004 Budget Speech*, moratoriums were introduced to assess the relevance of certain fiscal measures designed to encourage individuals to invest in Québec businesses, namely the Stock Savings Plan (SSP) and Québec Business Investment Companies (QBIC). The government also introduced a moratorium regarding tax assistance for major investment projects.

Concerning the SSP and QBICs, the government is currently reviewing the state's role in financing businesses. Accordingly, following the Brunet Report on the role of the Québec state in venture capital and the work of the Commission des finances publiques, a number of possible solutions have been suggested.

The government is in the process of identifying the approach it intends to take to support the capitalization of businesses. Until then, the moratoriums on these measures will be maintained.

Corporate taxation

5. Exemption from the tax on capital for SMEs raised from $600 000 to $1 million

The government's priority regarding corporate taxation is to reduce fixed charges that directly hamper investment and job creation. These charges have damaging effects on businesses, in particular in the start-up phase or when they are unable to generate a profit.

More specifically, the harmful effect on investment of the tax on capital has been abundantly documented. It increases the cost of investment, saps productivity and penalizes the manufacturing sector in particular.

That is why the government is continuing the effort it initiated in the last Budget Speech to eliminate this tax, focusing on SMEs to begin with.

Since January 1, 2004, almost 70% of Québec businesses have been exempt from the tax on capital because the exemption, i.e. the threshold below which this tax does not apply, was raised to $600 000.

This Budget Speech raises this exemption to $1 million as of January 1, 2005. Accordingly, another 15 000 SMEs will no longer pay this tax on their investments. In all, more than 75% of Québec businesses will be totally exempt from the tax on capital.

TABLE 16

EXEMPTION REGARDING THE TAX ON CAPITAL, AND NUMBER OF TOTALLY EXEMPT BUSINESSES

	2003	2004	2005
▪ Exemption[1] (dollars)	250 000	600 000	1 000 000
▪ Number of exempt businesses	162 000	195 000	210 000
▪ As a percentage of all businesses	58.1	69.8	75.4

1 For the years 2003 to 2005, a total exemption applies to SMEs whose paid-up capital is below these amounts. The value of the exemption gradually declines for SMEs whose paid-up capital is above the exemption and below $1 million in 2003, $2.4 million in 2004 and $4 million in 2005.

Source: Ministère des Finances du Québec.

The net impact of this relief measure will be $74 million over a full year.

Conclusion

In the *2003-2004 Budget Speech*, the government announced a review of all tax expenditures.

After examining their scope and efficiency, the government is completing, with this Budget Speech, its review of tax expenditures. This most recent stage has confirmed the tax assistance for R&D, improved certain measures, in particular for the development of the regions and, lastly, introduced a number of tightening measures.

The *2004-2005 Budget Speech* also provides an opportunity to take another step for Québec SMEs. Accordingly, the increase of the exemption threshold from the tax on capital to $1 million will spur them to carry out new investments.

TABLE 17

FISCAL MEASURES PERTAINING TO BUSINESSES
FINANCIAL IMPACT FOR THE GOVERNMENT
(Millions of dollars)

	Full year	2004-2005	2005-2006
REVIEW OF TAX EXPENDITURES			
1. Enhancing certain fiscal measures			
▪ Tax credits for processing activities in the resource regions	-12	-7	-10
▪ Cooperative Investment Plan	-11	-1	-7
▪ Tax credit for on-the-job training periods	-3	-2	-3
▪ Tax credit for new graduates working in a remote resource region	-13	-3	-13
▪ Flow-through share system	-8	-2	-6
▪ Tax credit for resources	-2	-1	-2
▪ Tax credit for technology adaptation services	-1	-1	-1
▪ Tax credit for film and television production	-10	-10	-10
▪ Relief measure applicable to the ceiling applicable to entertainment expenses	-3	-3	-3
Subtotal – enhancements	-63	-30	-55
2. Tightening certain fiscal measures			
▪ International financial centres	25	6	18
▪ Tax-assisted funds	34	3	30
▪ Deductibility of investment expenses	28	8	28
▪ Deduction for securities options	13	-	13
3. Eliminating certain fiscal measures			
▪ Five-year tax holiday for new corporations	75	8	30
▪ Tax credit for railway businesses	12	4	11
Subtotal – tightening measures	187	29	130
CORPORATE TAXATION			
▪ Increase in the exemption from the tax on capital for SMEs	-74	-17	-74
Subtotal – corporate taxation	-74	-17	-74
FINANCIAL IMPACT FOR THE GOVERNMENT	**50**	**-18**	**1**